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No.

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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1995

PROMETHEUS FUNDING CORP., etc., et al.,
Petitioners,

VS.

MERCHANTS HOME DELIVERY SERVICES, INC.,
Respondent.

Petition For Writ of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The relevant provision of the McCarran-Ferguson Act [15 U.S.C. Section 1012(b)] provides that "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any state for the purpose of regulating the business of insurance." Under this provision:

1. Does the assertion of claims under the Racketeer Influenced and Corrupt Organizations Act (RICO) based on activities which constitute the business of insurance "invalidate, impair, or supersede" comprehensive state laws enacted for the express purpose of regulating the business of insurance where RICO imposes treble damages and attorney fee awards but such damages and awards are unavailable under state law?

2. Does the phrase "enacted . . . for the purpose of regulating the business of insurance" apply narrowly so that a transfer of risk from the insured to an insurer is required or does it apply more broadly to encompass activities that are integral to the business of insurance and are made possible only because the business of insurance was at the heart of the transactional relationship between the parties?

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PARTIES TO PROCEEDINGS AND DISCLOSURE STATEMENT

This petition is filed by Prometheus Funding Corp., which was formerly known as Frank B. Hall & Co. Inc. The petition is also filed by Frank B. Hall Insurance Brokers, Inc., a subsidiary of Prometheus Funding Corp. Frank B. Hall of California was a subsidiary of Frank B. Hall & Co. Inc. In 1990, Frank B. Hall of California was merged into Frank B. Hall Insurance Brokers, Inc. The operating assets of Frank B. Hall & Co. Inc. were sold to petitioner AON Corporation in November 1992. Other petitioners are Rollins Hudig Hall, and Rollins Hudig Hall of Southern Cali-

fornia, Inc., which are insurance broker subsidiaries of AON Corporation.

Petitioners also disclose the following related companies: Prometheus Funding Corp. is a wholly-owned subsidiary of Reliance Group Holdings, Inc.

PETITION

Petitioners respectfully pray that a writ of certiorari issue to review the judgment of the Court of Appeals for the Ninth Circuit, entered March 28, 1995. Petitioners' petition for rehearing and suggestion for rehearing en banc was denied by the Court of Appeals on June 8, 1995.

I

OPINIONS BELOW

The opinion of the Ninth Circuit (App. 14a-25a) is reported at 50 F.3d 1486 (9th Cir. 1995). The district court's order granting petitioners' motion for judgment on the pleadings is not officially reported and is reproduced in the Appendix at pages 1a-10a.

II

JURISDICTION

The Court of Appeals entered its judgment on March 28, 1995. The Court of Appeals denied petitioners' timely petition for rehearing and suggestion for rehearing en banc on June 8, 1995. (App. 11a-13a) The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1). The Court of Appeals' jurisdiction was based on 28 U.S.C. Section 1291, and the district court's jurisdiction was invoked under 28 U.S.C. Section 1331.

III

STATUTORY PROVISIONS INVOLVED

The relevant provisions of the McCarran-Ferguson Act state:

15 U.S.C. § 1011:

> Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

15 U.S.C. § 1012:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

The relevant provision of the federal Racketeer Influenced and Corrupt Organization Act (18 U.S.C. § 1961 *et seq.*) (RICO) is section 1964, which is set forth in the Appendix at page 26a.

The California Unfair Insurance Practices Act (Cal. Ins. Code § 790 *et seq.*) is set forth in the Appendix at pages 27a-39a.

IV

STATEMENT OF CASE

In January 1986, Merchants Home Delivery Services, Inc. (Merchants) and two individuals, who were reportedly acting on behalf of Frank B. Hall & Co. of California, entered into an agreement for the provision of comprehensive insurance and related risk management services. (Appellant's Excerpts of Record [ER], filed with the Ninth Circuit Court of Appeals, at 14, 44-64) These individuals, acting as exclusive insurance brokers for Merchants, provided, or at least purported to provide, a complete package of insurance services, including negotiating and placing casualty insurance, supervising all underwriting and claims functions, managing and adjusting claims, and invoicing all premiums and "paid loss" billings from the insurers. (ER 14-15, 66) However, the two individuals involved allegedly were defrauding Merchants by overcharging for the insurance coverage obtained, charging for coverage that never was obtained, and overcharging for handling and resolving various self-insured claims. (ER 15-17, 20-24) Two employees of Frank B. Hall & Co. Inc. were later convicted of grand theft, in part because of activities related to the Merchants account.

After petitioners discovered the employees' activities, the employees were terminated and their activities were reported to Merchants. Merchants then sued petitioners in federal district court, seeking money damages based on several state law causes of action and alleging violations of the federal RICO statute. (ER 1-42) Based on the RICO allegations, Merchants sought an award of treble damages and attorney fees. (ER 40-42) See 18 U.S.C. § 1964(c).

The district court first declined to exercise jurisdiction over the state law claims and then dismissed the RICO claims on the ground that, under the McCarran-Ferguson Act, they could not be asserted against entities engaged in the business of insurance.[1] (App. 1a-10a) As the district court explained, McCarran-Ferguson barred application of RICO in this case because California has a comprehensive regulatory scheme for the business of insurance that expressly regulates all forms of insurance brokerage activities and prohibits fraud in connection with those activities. (App. 9a-10a) California law, however, does not permit awards of the treble damages and attorney fees that are mandatory under RICO. (App. 10a) In reaching this conclusion, the district court followed a California Court of Appeal decision that reached the same result for the same reasons. *American Int'l Group, Inc. v. Superior Court*, 285 Cal. Rptr. 765 (Ct. App. 1991), *review denied*, (Cal. Sup. Ct. Dec. 12, 1991), *cert. denied sub nom., Brutoco Engineering & Const. v. American Int'l Group, Inc.*, 504 U.S. 911 (1992). (App. 4a)

The Court of Appeals for the Ninth Circuit reversed. (App. 14a-25a) The Court first held that not all of the activities targeted by the RICO claims constituted the business of insurance. (App. 19a-22a) According to that Court, the business of insurance does not exist unless there has been a transfer of risk from the insured to an insurer accomplished by the issuance of an insurance policy. (App. 20a) Thus, of the allegedly fraudulent activities de-

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[1] While this litigation over the validity of the RICO claims was occurring, Merchants filed a parallel action in California state court. In that action, which petitioners asked the Ninth Circuit to judicially notice, Merchants alleged 23 causes of action against petitioners and other defendants and sought treble damages and attorney fees on various theories. However, the state trial court granted petitioners' motion to strike all claims for those remedies, thus confirming that the remedies available under RICO are not available to Merchants under California law.

scribed in the complaint, the Court found that only the overcharging for premiums on policies that actually existed was within the business of insurance. (App. 20a-21a) In contrast, the Court concluded that the business of insurance did not include charging for premiums for policies that did not exist or charging for fictitious claims for which Merchants was self-insured. (App. 21a-22a)

The Court of Appeals next held that, even as to the activities that were within the business of insurance, McCarran-Ferguson would not bar application of RICO. (App. 22a-25a) In so holding, the Court followed the reasoning of *NAACP v. American Family Mutual Ins. Co.*, 978 F.2d 287 (7th Cir. 1992), *cert. denied*, 113 S. Ct. 2335 (1993), which held that, under McCarran-Ferguson, there must be a direct conflict between federal and state law before that federal law would "invalidate, impair, or supersede" the state law. (App. 24a-25a) Based on this analytical model, the Ninth Circuit found that federal law did apply to activities within the business of insurance, even when those activities were extensively regulated by the states, so long as the remedies provided by federal law merely duplicated or were consistent with the remedies available under state law. (App. 25a) The Ninth Circuit thereafter reasoned that McCarran-Ferguson presented no bar to the RICO claims asserted by Merchants because the alleged fraud was prohibited by state as well as federal law. (App. 25a)

Petitioners sought rehearing and made a suggestion for rehearing en banc because: (1) the Ninth Circuit's holding that federal law had to conflict directly with state law before McCarran-Ferguson would apply could not be reconciled with this Court's decisions; (2) the Ninth Circuit's reasoning added to the confusion in this area of the law by disagreeing with the many state appellate court and federal district court decisions holding that McCarran-Ferguson does bar application of RICO to activities that are within

the business of insurance; and (3) the Ninth Circuit's holding that an activity could not be part of the business of insurance unless it effected a transfer of risk through an insurance policy also was at odds with this Court's interpretation of McCarran-Ferguson and will create uncertainty in this area of the law.

The Ninth Circuit denied petitioner's petition for rehearing and suggestion for rehearing en banc, although one judge voted in favor of rehearing en banc. (App. 11a-13a)

V

REASONS TO GRANT THE WRIT

In enacting McCarran-Ferguson five decades ago, Congress gave the states supremacy with respect to regulation of the business of insurance. In order to protect the states' ability to regulate the business of insurance, Congress provided that *unless* it expressly intended to have one of its laws apply to the business of insurance, that law could *not* be applied to "invalidate, impair, or supersede" a state law enacted for the purpose of regulating the business of insurance. The Ninth Circuit's opinion here, however, frustrates Congress' intent in two fundamental respects and, by doing so, invites the broad application of federal law to the business of insurance — the precise result Congress sought to forestall with the passage of McCarran-Ferguson.

First, the Ninth Circuit's opinion holds that federal laws such as RICO can always apply in tandem with state laws regulating the business of insurance so long as federal law does not actually conflict with state law. That holding cannot be reconciled with the reasoning in this Court's decisions, exacerbates an existing conflict in the case law, and is contrary to the relevant statutory language.

Second, the Ninth Circuit's opinion ascribes a narrow meaning to the phrase "business of insurance," so that many

activities normally associated with the business of insurance are deemed outside McCarran-Ferguson's scope and thus subject to regulation by federal law. That holding also conflicts with one of this Court's key decisions and will produce uncertainty in this area of law.

This Court therefore should grant certiorari to resolve these conflicts and provide needed guidance on the proper application of McCarran-Ferguson.

A. Whether RICO Claims Can Be Asserted Against Entities Engaged In The Business Of Insurance Is An Issue Of Nationwide Importance Implicating Paramount Federal Statutory Policies On Which There Is A Conflict In The Cases

1. The Ninth Circuit's Opinion Finding That RICO Claims Are Not Preempted By McCarran-Ferguson Is In Apparent Conflict With Decisions By This Court And Exacerbates A Conflict In The State Appellate Courts And In The Federal District Courts On Whether RICO Claims Are Preempted

The Ninth Circuit's opinion asserts that McCarran-Ferguson's bar against application of federal law to the business of insurance applies only where the federal law in question actually or directly conflicts with state law. But this Court has never said that such an actual or direct conflict is needed to come within McCarran-Ferguson and the Court of Appeals' opinion is in apparent conflict with this Court's important McCarran-Ferguson decisions. What is more, the opinion sharpens and exacerbates the conflict among courts nationwide on whether McCarran-Ferguson bars application of RICO to the business of insurance.

By way of background, Congress enacted the McCarran-Ferguson Act almost immediately after this Court held in

United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533 (1944), that the business of insurance was within the reach of the Commerce Clause and thereby subject to regulation under federal law. Because that decision threatened to undermine the states' historical primacy over insurance, "Congress moved quickly to restore the supremacy of the states in the realm of insurance regulation." *United States Dep't of Treasury v. Fabe*, 113 S. Ct. 2202, 2207 (1993); *see also Prudential Ins. Co. v. Benjamin*, 328 U.S. 408, 429 (1946). Indeed, McCarran-Ferguson "transformed the legal landscape" where the regulation of the business of insurance is concerned by "overturning the normal rules of preemption." *Fabe*, 113 S. Ct. at 2211. In doing so, Congress (1) expressly declared that the states have primary jurisdiction to regulate the business of insurance [15 U.S.C. Section 1012(a)], and (2) expressly reversed the ordinary preemptive effect of federal law in favor of state law preemption of federal law where the state law is "enacted for the purpose of regulating the business of insurance" [15 U.S.C. Section 1012(b)].[2]

Senator Ferguson, one of the authors of the Act, explained its effect as follows:

> If there is on the books of the United States a legislative act which relates to interstate commerce, if the act does not specifically relate to insurance, it would not apply at the present time. Having passed the bill now

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[2]The lower federal courts have developed a four-part test for determining whether McCarran-Ferguson applies: (1) does the federal law in question specifically relate to the business of insurance; (2) do the activities at issue constitute the business of insurance; (3) has the state enacted laws for the purpose of regulating the business of insurance; and (4) if so, would the application of the federal law "invalidate, impair, or supersede" the state law. *Cochran v. Paco, Inc.*, 606 F.2d 460, 464 (5th Cir. 1979). As to at least some of the allegations involved here, there is no question that the first three parts of the test are satisfied.

> before the Senate, if Congress should tomorrow pass a law relating to interstate commerce, and should not specifically apply the law to the business of insurance, it would not be an implied repeal of this bill [the McCarran-Ferguson Act] . . .

Cochran v. Paco, Inc., 606 F.2d at 463 n. 7, quoting 91 Cong. Rec. 481 (1945); *see also Fabe,* 113 S. Ct. at 2211 n. 7 (quoting similar remarks).

This Court examined the "invalidate, impair, or supersede" prong of McCarran-Ferguson in *Securities & Exch. Comm'n v. National Secs., Inc.*, 393 U.S. 453 (1969) (*SEC*). There, the SEC sought to unwind a merger between two insurance companies that Arizona's Director of Insurance had approved because it did not harm the interests of policyholders. Although this Court held that McCarran-Ferguson was not a bar to that action, *SEC*'s rationale is at odds with the Ninth Circuit's reasoning and supports the opposite result here. In particular, this Court explained that Arizona's interest in protecting *policyholders* affected by the merger was much narrower than the SEC's important and broader interest in protecting the companies' *shareholders* (many of whom would not also be policyholders) who were harmed by a merger brought about through allegedly false representations. Thus, this Court held that this potential interference with a state law regulating insurance to be too "indirect" to be an obstacle to the pursuit of the "paramount federal interest" in regulating the securities markets. But at the same time, this Court cautioned that "[d]ifferent questions would, of course, arise if the Federal Government were attempting to regulate in the sphere reserved primarily to the States by the McCarran-Ferguson Act." *Id.* at 463.

The only other decision by this Court that touches on these issues is *Federal Trade Comm'n v. National Cas. Co.*, 357 U.S. 560, 563-64 (1958) (*FTC*), where this Court addressed whether the Federal Trade Commission could

regulate an insurance company's allegedly unfair and deceptive advertising practices carried out in states that had their own statutes regulating those practices. This Court held that the FTC could not, rejecting its claims that Congress had not intended to preclude application of federal law as a "supplement" to state action and that a state's "general regulation" of unfair practices should not supplant federal law. *Id.*

In contrast to these cases, the Ninth Circuit rejected application of McCarran-Ferguson even though Merchants is asserting RICO claims based on activities that are well within the "sphere" of the insurance regulatory concerns that McCarran-Ferguson commits "primarily to the States." California's comprehensive regulatory scheme applies here precisely because Merchants has alleged that fraud was committed in the course of the business of insurance, and there can be no question that California is committed to the prevention of fraud in such circumstances. *See, e.g.,* Cal. Ins. Code §§ 780 (prohibits brokers from making misrepresentations about terms and conditions of policy); 790.03(a) (prohibiting misrepresentations regarding terms and benefits of a policy); 790.03(b) (broad prohibition regarding misrepresentations in any public statement about the nature of a person's insurance business); 790.035 (authorizing civil penalties for committing any unfair practice).

Yet RICO applies, if at all, for exactly the same reasons — the alleged commission of fraud in circumstances where the insurance business activities involved are further claimed to constitute a RICO "enterprise." (ER 19-25) But in contrast to *SEC*, application of RICO in such circumstances does not further any "paramount federal interest." *See Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 240-42 (1987) (refusing to exempt civil RICO claims from Federal Arbitration Act in part because there is no overriding national interest in the deterrent aspects of a

"run-of-the-mill civil RICO" claim when asserted against a "legitimate" business). On the contrary, under the express mandate of McCarran-Ferguson the business of insurance is for the states to regulate without the intrusion of federal law.[3] *Fabe*, 113 S. Ct. at 2207. Moreover, application of RICO to the conduct alleged here does directly intrude into California's regulation of the business of insurance by providing mandatory remedies that are unavailable under California law. *American Int'l Group*, 285 Cal. Rptr. at 777; *see* discussion *infra* at pp. 14-17, 20-22.

The stark difference in approach to McCarran-Ferguson between *SEC* and the Ninth Circuit's opinion is amplified by appellate decisions from California and Pennsylvania. *American Int'l Group*, 285 Cal. Rptr. 765; *Leckey v. Aetna Cas. & Sur. Co.*, 590 A.2d 1255 (Pa. Super. Ct. 1991). Both cases hold that McCarran-Ferguson bars RICO claims because the assertion of even allegedly compatible federal law theories will "invalidate, impair, or supersede" state laws regulating the business of insurance. As the California Court of Appeal explained, permitting a RICO claim "for the very conduct which California has chosen to regulate administratively would subvert and subsume the existing

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[3] Commentators agree with this interpretation of McCarran-Ferguson and summarize the teaching of this Court's decisions as follows:

> [S]tate regulation of the business of insurance is considered to oust federal regulation when the state has adopted effective regulations specifically relating to the subject matter addressed by the federal regulatory scheme (whether or not the state law is as stringent as federal law). Federal regulation also is considered precluded when the state has regulated the business so comprehensively as to occupy the field of insurance regulation, even if the state does not have a specific regulation directed to the matter which the federal regulation is attempting to control.

Jonathan R. Macey & Geoffrey P. Miller, *The McCarran-Ferguson Act: Reconceiving The Federal Role Of Insurance Regulation*, 68 N.Y.U.L. Rev. 13, 30 (1993).

statutory scheme. It would permit a civil damage recovery where [the California] Supreme Court has recently and explicitly held that none was intended." *American Int'l Group*, 285 Cal. Rptr. at 777. The Ninth Circuit nevertheless ignored this California court's view of what the impact of RICO would be on California's regulation of the business of insurance.

Federal district court decisions reveal the same sharp conflict and also confirm that the question whether RICO claims may be aimed at the business of insurance is a frequently recurring issue at the forefront of McCarran-Ferguson jurisprudence. *Compare Wexco Inc. v. IMC, Inc.*, 820 F. Supp. 194 (M.D. Pa. 1993) (holding that McCarran-Ferguson precludes application of RICO), and *Gordon v. Ford Motor Credit Co.*, 868 F. Supp. 1191 (N.D. Cal. 1992) (same), *with Moore v. Fidelity Fin. Serv., Inc.*, 884 F. Supp. 288, 292-93 (N.D. Ill. 1995) (holding that RICO claims are possible despite McCarran-Ferguson); *Thacker v. New York Life Ins. Co.*, 796 F. Supp. 1338 (E.D. Cal. 1992) (same). To date a majority of district court decisions have held that RICO should *not* apply to the business of insurance.[4]

In light of this deep division in the cases, it is unlikely that other courts will uniformly follow the Ninth Circuit's opinion here, thus resolving the conflict without the need for this Court to intervene. In fact, the district court for the Eastern District of Virginia has already refused to follow the Ninth Circuit, explaining that the Ninth Circuit's reasoning is flawed and results in an unduly restrictive interpretation of

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[4] *E.g., Forsyth v. Humana, Inc.*, 827 F. Supp. 1498, 1520-22 (D. Nev. 1993); *Senich v. Transamerica Premier Ins. Co.*, 766 F. Supp. 339, 341-42 (W.D. Pa. 1990); *Everson v. Blue Cross & Blue Shield*, No. 93CV7534, 1994 WL 675200, *12-13 (N.D. Ohio 1994); *Richhart v. Metropolitan Life Ins. Co.*, 1990 U.S. Dist. LEXIS 3597, *5-7 (E.D. Pa. 1990).

the McCarran-Ferguson Act. *Ambrose v. Blue Cross & Blue Shield of VA, Inc.*, ____ F. Supp. ____, 1995 WL 385165, *15-16 (E.D. Va. 1995); *see infra* at pp. 18-20.

This pronounced conflict in the cases concerning the application of an important federal statute deserves this Court's attention, and it is a question of "when," not "if," this Court will have to take up the issue and resolve the conflict. Until resolved, however, that conflict will result in the uneven and arbitrary application of McCarran-Ferguson, for whether RICO can be applied in this context often will be dictated merely by whether a lawsuit is filed in federal court, which may follow the opinion here, or a state court, which may follow cases such as *American Int'l Group*.

This Court should act now to forestall a proliferation of conflicting decisions, provide the guidance the lower state and federal courts need, and avoid countless hours of litigation over the threshold question of whether RICO even applies. The issue is squarely presented here, is ripe for decision, and petitioners therefore respectfully urge this Court to grant certiorari.

2. The Ninth Circuit's Opinion Misconstrues McCarran-Ferguson, Resulting In An Erroneous Expansion Of Federal Authority Over The Business Of Insurance

Although the conflict in the cases alone warrants this Court's attention, certiorari also is warranted because the Court of Appeals' narrow reading of the phrase "invalidate, impair, or supersede" does not withstand scrutiny as a matter of statutory construction and thus distorts the meaning and effect of an important federal law. Under the plain meaning of the statutory language, there does not have to be an actual or a direct conflict between federal law and a state law which regulates the business of insurance before McCarran-Ferguson applies.

" '[T]he starting point in a case involving construction of the McCarran-Ferguson Act, like the starting point in any case involving the meaning of a statute, is the language of the statute itself.' " *Fabe*, 113 S. Ct. at 2207-08. To be sure, application of such a directly conflicting federal law would "invalidate, impair, or supersede" state law. But if Congress had intended to bar application of only conflicting federal laws, it would have said so directly. Instead, McCarran-Ferguson is couched in terms that must carry a broader meaning than direct conflict. The word "impair" means "to damage, injure, diminish, prejudice, undermine or weaken." *Brownell v. State Farm Mut. Ins. Co.*, 757 F. Supp. 526, 536 n. 13 (E.D. Pa. 1991) (citing Webster's New Collegiate Dictionary (9th ed. 1988) and Webster's Collegiate Thesaurus (1976)). The word "supersede" connotes making something "superfluous or unnecessary" by supplanting it with something else. Webster's Third New International Dictionary 2295 (1986). In light of these ordinary and accepted meanings of the words Congress used instead of "direct conflict," the routine assertion of RICO claims, which will be inevitable following the Ninth Circuit's opinion, will of necessity impair and supersede state regulatory schemes.

California and all but a few other states rely on a comprehensive mix of statutory and common law principles, enforced by administrative and private actions, to regulate the business of insurance. *See Manufacturers Life Ins. Co. v. Superior Court*, 41 Cal. Rptr. 2d 220, 230-31 (Cal. 1995); *Moradi-Shalal v. Fireman's Fund Ins. Cos.*, 250 Cal. Rptr. 116, 121 (Cal. 1988). In California, for example, the Legislature expressly intended to regulate the business of insurance to the greatest extent possible under McCarran-Ferguson. Cal. Ins. Code § 790; *Manufacturers Life Ins. Co.*, 41 Cal. Rptr. 2d at 229 (California's Unfair Insurance Practices Act was enacted with the "acknowledged purpose . . . to preclude federal jurisdiction over the business of insurance"). To that end, California's Unfair Insurance

Practices Act lists the types of practices that are proscribed and contains a full remedial scheme exclusively administered by the Department of Insurance. *See* Cal. Ins. Code §§ 790.03 *et seq.*; *Moradi-Shalal*, 250 Cal. Rptr. at 126 (holding that violation of these statutes does not give rise to an implied right of action); *see also American Int'l Group*, 285 Cal. Rptr. at 777. This regulatory scheme also exists on top of the full panoply of common law rights and remedies afforded by California law — rights that Merchants is presently pursuing in state court. (*See supra* p. 5, n. 1) Given these layers of California law effectively regulating the business of insurance, this Court cannot assume that the California Legislature anticipated, or would approve of, the addition of another layer of federal remedies — such as treble damages and attorney fees — it did not see fit to provide.[5] *See American Int'l Group*, 285 Cal. Rptr. at 777; *Gordon*, 868 F. Supp. at 1196-97; *Forsyth*, 827 F. Supp. at 1520-22.

Consequently, the availability of a mandatory award of treble damages and attorney fees under RICO [18 U.S.C. § 1964(c)] would significantly reduce the need for a litigant to rely on state laws that regulate the business of insurance. But where state law is not invoked, or at least takes a back seat to federal law, a state's ability to regulate the business of insurance effectively is jeopardized. In that sense, the routine application of RICO would necessarily supplant state law by diminishing its importance as the primary

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[5]The result does not change because punitive damages are available in California. Punitive damages are discretionary, vary in amount, and can be imposed only if the plaintiff meets a rigorous statutory standard by clear and convincing evidence. *See* Cal. Civ. Code § 3294; *College Hosp., Inc. v. Superior Court*, 34 Cal. Rptr. 2d 898, 908 (Cal. 1994); *Adams v. Murakami*, 284 Cal. Rptr. 318, 320-21 (Cal. 1991).

source for regulation of the business of insurance.[6] That impact on state law, in turn, is all that is — or should be — required for McCarran-Ferguson to apply. *American Int'l Group,* 285 Cal. Rptr. at 777; *Ambrose,* 1995 WL 385165, *15 ("the disparity between the cause of action and remedy permitted by RICO and the enforcement mechanism and remedy permitted by Virginia's insurance code [is] so great that the federal law would in fact supersede the state law"); *see Fabe,* 113 S. Ct. at 2207 (McCarran-Ferguson enacted because Congress wanted to "restore the supremacy of the states" with respect to regulation of the business of insurance).

The Ninth Circuit apparently bypassed this analysis, however, and relied instead on the Seventh Circuit's *NAACP* decision as the sole authority for its holding that McCarran-Ferguson did not preempt civil RICO claims aimed at the business of insurance. That reliance was misplaced because the reasoning in *NAACP* is flawed. The question in *NAACP* was whether McCarran-Ferguson barred application of the federal Fair Housing Act (FHA) to insurance companies that allegedly engaged in "redlining" when issuing homeowners insurance policies. One part of the opinion focused on whether application of the FHA would "invalidate, impair, or supersede" the relevant state law. In that regard, the *NAACP* Court started with the

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[6]Merchants and its amici have argued here that the availability of RICO claims will actually assist the states in regulating improper insurance practices. That argument begs the question, for it is not grounded in the language or history of the McCarran-Ferguson Act. Indeed, if the states truly need more assistance, then the answer is not to pretend that McCarran-Ferguson is an anachronism in the law. Rather, the answer would be to persuade Congress to repeal McCarran-Ferguson, amend RICO to expressly apply it to the business of insurance, or enact other laws that have the specific purpose of regulating the business of insurance. *See* 15 U.S.C. Section 1013 (exempting certain laws from the impact of McCarran-Ferguson).

premise that "even thoroughgoing federal regulation" usually does not impliedly preempt state law regulating the same activity. 978 F.2d at 296. It then stated — without offering any supporting analysis — that because the "McCarran-Ferguson Act is a form of inverse preemption . . . principles defining when state remedies conflict with (and so are preempted by) federal law are pertinent," *Id.*

But in so framing the issue it decided, the *NAACP* Court overlooked the fundamental differences between implied preemption principles on the one hand and McCarran-Ferguson on the other. *See Ambrose*, 1995 WL 385165, *16. When the question is whether federal law impliedly preempts state law, the courts routinely *presume* that state law may regulate the conduct in question unless the party urging implied preemption shows that state law actually conflicts with the goals and objectives of federal law. *California v. ARC America Corp.*, 490 U.S. 93, 101 (1989); *Chemical Specialties Mfrs. Ass'n, Inc. v. Allenby*, 958 F.2d 941, 943 (9th Cir.), *cert. denied,* 113 S. Ct. 80 (1992). Because state sovereignty is at stake, absent such a conflict the courts uphold and respect state laws that may parallel federal law or provide additional rights and remedies. *E.g., English v. General Elec. Co.*, 496 U.S. 72, 82-90 (1990). These principles thus limit the scope of implied preemption and, by making it *more difficult* for federal law to preempt state law, make it *easier* for state law to apply alongside federal law.

The very purpose of McCarran-Ferguson, however, is to *reserve to the states* broad regulatory control over the business of insurance without the intrusion of general federal laws regulating various aspects of interstate commerce. *SEC,* 393 U.S. at 459; *Western & S. Life Ins. Co. v. State Bd. of Equal.*, 451 U.S. 648, 654 (1981); *see* discussion *supra* at pp. 8-10. In enacting McCarran-Ferguson, Congress indisputably intended to make it *easier* for the states to

regulate the business of insurance *without* federal encroachment and thereby to make it *more difficult* for federal law to apply alongside state law. *See Prudential Ins. Co.*, 328 U.S. at 429-30. Yet if McCarran-Ferguson preemption operates only when federal and state law actually or directly conflict, the effect will be to significantly reduce — not enlarge or enhance — the sphere of state sovereignty over the business of insurance.

Simply put, the *NAACP* Court asked the wrong question. In construing the phrase "invalidate, impair or supersede," a court cannot — and should not — stop with a determination that there is no "actual conflict" between state and federal law. Rather, because Congress wanted to enhance the likelihood that the states would be able to regulate the business of insurance without encroachment by federal law, logic and the holding of *FTC* show that a different analytical model must be employed for McCarran-Ferguson preemption. In that respect, the controlling law should be derived from cases involving express preemption.

In *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 53-54 (1987), for example, this Court construed ERISA's preemptive scope by emphasizing that Congress intended to provide a comprehensive system of rights and remedies for ERISA plan beneficiaries that had the effect of excluding state law rights and remedies, whether they be conflicting, parallel, or cumulative. *Cf. FTC*, 357 U.S. at 563 (McCarran-Ferguson preemption precludes even "supplemental" federal regulation). Further, because ERISA contained this comprehensive remedial scheme, these additional remedies unavoidably would interfere with and disrupt federal law. *Pilot Life*, 481 U.S. at 54. By analogy, therefore, the first question a court should ask in a McCarran-Ferguson case is whether the state has acted to comprehensively regulate the business of insurance. Where such a comprehensive scheme exists, cases like *Pilot Life* also show what the next step in

the analysis should be. A court should *not* assume that a state that has enacted a comprehensive regulatory system nevertheless contemplated that federal law would be imported to augment this regulatory framework whenever it could be characterized as not being in actual conflict with an express provision of state law. *Compare Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 386 (1992) (even consistent state law is expressly preempted by the Airline Deregulation Act because federal law is controlling); *Mackey v. Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825, 829 (1988) (same under ERISA).

By employing a flawed analytical approach, the Ninth Circuit's interpretation of McCarran-Ferguson will result in more, not less, federal regulation of the business of insurance. Not only will this flawed reasoning allow RICO claims to be asserted in cases like this one, but it will open the door to application of other federal laws that, although they have nothing to do with insurance, prohibit conduct which is also illegal under state law. That cannot have been the result Congress intended, but this expansion of federal sovereignty over the business of insurance will continue unabated until this Court acts. Certiorari is warranted for this reason as well.

3. The Ninth Circuit's Opinion Will Disrupt The States' Regulation Of Insurance And Frustrate The Intent Of Congress

There is a further and compelling need for this Court's review: The importance of the issue presented is underscored by the fact that the Court of Appeals' opinion goes a long way toward "federalizing" insurance disputes. Given the frequency with which RICO claims already have been alleged in insurance cases and are alleged in non-insurance actions, RICO counts will be standard items in what otherwise would be breach of insurance contract lawsuits

governed solely by state law. Experience shows that when given the choice, plaintiffs and their counsel will rarely, if ever, forego the opportunity to recover on a theory that mandatorily imposes treble damages and attorney fees. Further, because RICO provides federal question jurisdiction, the availability of that cause of action will, as in this case, be the sole reason why the federal district courts will increasingly become the forum for lawsuits like this one. (App. 2a, 10a) *E.g., Senich v. Transamerica Premier Ins. Co.*, 766 F. Supp. 339 (dismissing complaint containing state law claims for lack of federal jurisdiction after concluding that McCarran-Ferguson barred the plaintiff's RICO claims).

The inevitable effect of the Ninth Circuit's decision will be that McCarran-Ferguson will *not* bar this onslaught of RICO claims that involve the business of insurance and are made against insurance companies or insurance brokers. Thus, while Congress in effect chose a "hands off" policy toward the regulation of the business of insurance, the opinion here makes Congress and the federal courts de facto regulators of that activity. This "federalization" of insurance litigation is plainly irreconcilable with the express purpose of McCarran-Ferguson. (*See supra pp. 8-10*)

At the same time, insurance companies and insurance brokers will now face considerable uncertainty over what federal laws may apply in addition to state laws regulating the business of insurance. Given the Ninth Circuit's approach, an insurer's and insurance broker's compliance with state law will no longer provide them with the assurance that they have fully complied with the law, and they must at least consider all federal laws that may not conflict with state law but nevertheless represent an additional layer of insurance regulation. That will be true, moreover, even though Congress did not enact these laws contemplating that they would be applied to regulate the business of insurance.

Finally, subjecting insurers and insurance brokers to RICO's threat of treble damages and attorney fees — threats they usually do not face under state law — cannot help but disrupt the insurance market by driving up the cost of insurance. Even if the likelihood of exposure in a RICO claim is low, the mere potential for a crushing damages award will compel insurers to settle claims they otherwise could have successfully defended. Those extra settlements will exact their own costs in the form of increased premiums for other insureds. *See Garvey v. State Farm Fire & Cas. Co.*, 257 Cal. Rptr. 292, 299 (Cal. 1989). Because the cost of insurance is central to the states' regulation of insurance, the imposition of new and costly forms of liability ought to come from the states — not from Congress — at least where Congress has merely enacted a law of general applicability rather than one aimed at the business of insurance.

The applicability of McCarran-Ferguson in this context presents a question of nationwide importance to the states' ongoing ability to regulate the business of insurance as Congress intended. Unless this Court acts, there will be a sea change in how the courts apply McCarran-Ferguson. Unless this Court acts, Congress and the federal courts are going to become — virtually by default — active regulators of the business of insurance. The importance of these questions likewise justifies granting certiorari.

B. Whether The Phrase "Business Of Insurance" Should Be Narrowly Construed, Thereby Making Congress And The Federal Courts De Facto Regulators Of The Business Of Insurance, Is An Issue Of Nationwide Importance On Which There Is A Conflict In The Cases

Certiorari is also warranted to examine the Ninth Circuit's holding that the "business of insurance" is present for

purposes of McCarran-Ferguson only if there is an actual transfer of risk from the insured to an insurer. According to the Court of Appeals, the handling of self-insured claims and charging for policies that did not exist could not be part of the business of insurance because standing alone those activities did not result in a transfer of risk. That holding appears to be in conflict with this Court's decision in *Fabe*, and this Court should review the Ninth Circuit's opinion before its approach erroneously restricts application of McCarran-Ferguson in other cases.

1. The Ninth Circuit's Opinion Is In Apparent Conflict With This Court's Decision In *Fabe* Because It Narrowly Interprets The Phrase "Business Of Insurance" To Always Require A Transfer Of Risk

The question in *Fabe* was whether a state statute that determined the order of priority of claims in the event of an insurer's insolvency was a law enacted "for the purpose of regulating the business of insurance." *See* 15 U.S.C. § 1012(b). In analyzing that issue, this Court held there was a significant difference between that phrase and the antitrust proviso in the second part of Section 1012(b), which refers only to the "business of insurance."[7] Because of this difference in statutory language, a law enacted "for the purpose of regulating the business of insurance" is broader in scope than the business of insurance itself, and includes those laws that "possess the 'end, intention, or aim' of adjusting,

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[7]Where the antitrust proviso is involved, the question whether an activity is within the scope of the "business of insurance" requires consideration of a three-part test: (1) whether the practice has the effect of transferring or spreading a policyholder's risk; (2) whether the practice is an integral part of the policy relationship between the insurer and insured; and (3) whether the practice is limited to entities within the insurance industry. *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129 (1982); *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 210 (1979).

managing or controlling the business of insurance." *Fabe*, 113 S. Ct. at 2210, quoting Black's Law Dictionary 1236, 1286 (6th ed. 1990). Further, in this context the focus should be on the overall relationship between the policyholder and the insurer, which contemplates more than the bare issuance of an insurance policy. *Fabe*, 113 S. Ct. at 2208; *see SEC*, 393 U.S. at 460 ("Statutes aimed at protecting or regulating [the policyholder-insurance company] relationship, directly or indirectly are laws regulating the 'business of insurance.' ")

Under *Fabe*'s holding and approach, there seems little question that the parties' relationship and the insurance brokerage activities involved here directly or indirectly implicated the business of insurance and were made possible only because petitioners were engaged in the business of insurance. This plainly is *not* a situation where the only activity involved was claims handling for a self-insured entity or some other transaction that is completely on the periphery of the business of insurance. *Compare Moore v. Provident Life & Acc. Ins. Co.*, 786 F.2d 922 (9th Cir. 1986) (insurer was acting solely as a third-party administrator for a labor union's self-funded health benefits plan). Rather, as the district court emphasized, Merchants' complaint makes it clear that it authorized the two individuals involved to act as its exclusive insurance brokers precisely because they could negotiate, place and oversee insurance coverage as well as provide related risk management services. (*See* ER 14-15) *All* the misconduct alleged here occurred while delivering services that were part of the business of insurance. Further, those alleged acts of misconduct *are* subject to California's statutory scheme, which without question has the "end, intention, or aim" of regulating the business of insurance. *See* Cal. Ins. Code § 790 *et seq.*; *Manufacturer's Life Ins. Co.*, 41 Cal. Rptr. 2d at 229.

Fabe and the Ninth Circuit's opinion point in different directions. *Fabe* makes it clear that a court must consider the overall relationship between the parties and that a law can be enacted "for the purpose of regulating the business of insurance" even though the act regulated by itself does not transfer risk. The Ninth Circuit, in contrast, looks at the relationship piecemeal, so that the sum of its parts is less than the whole. By artificially circumscribing the scope of laws enacted for "the purpose of regulating the business of insurance," that piecemeal approach will minimize the states' role in regulating the business of insurance, contrary to *Fabe* and McCarran-Ferguson.

2. The Ninth Circuit's Opinion Will Create Confusion And Uncertainty In An Area Where Congress Has Mandated Certainty And Predictability Through State Regulation

By disregarding the overall context in which the alleged acts of misconduct took place, the Ninth Circuit's insistence that the business of insurance exists only if the activity involved directly relates to an existing insurance policy will lead to more unnecessary and troublesome confusion over when insurance activities are part of the business of insurance.

Here, for example, the Ninth Circuit correctly held that fraudulent premium overcharges were part of the business of insurance. Another court could, however, justify the opposite result by reasoning that the excessive portion of the premium, which should never have been charged in the first place, really transferred no risk at all. Following the approach of the Ninth Circuit's opinion here, a court could also conclude that the business of insurance was not involved where an insurer or broker allegedly misrepresented that a policy would cover a certain risk on the ground that, as to that risk only, no transfer of risk actually occurred. The same could be said anytime particular coverages are can-

celled, withdrawn, changed or erroneously represented to be available or unavailable. In each instance, the discrete acts involved do not literally involve the transfer of risk, but there can be no dispute that the business of insurance is involved.

Just as with the RICO issue, the Ninth Circuit's construction of the "business of insurance" issue finds no support in this Court's decisions, will produce confusion over the scope of McCarran-Ferguson, and will engender litigation over whether traditional insurance and risk management activities are within the business of insurance. Because conflicting rulings are sure to follow, this Court should grant certiorari to make clear that it meant what it said in *Fabe* and to put McCarran-Ferguson law back on its proper course.

VI

CONCLUSION

Petitioners respectfully urge this Court to grant certiorari in order to resolve conflicts in the cases and to provide clarity in this important area where state and federal law intersect. The questions presented here are at the core of the fundamental purposes of the McCarran-Ferguson Act, and whether RICO can be applied to the business of insurance is one of the most frequently litigated issues under that Act today. Further, the reasoning of the Court of Appeals' opinion conflicts with this Court's opinions on the scope of the McCarran-Ferguson Act, exacerbates a nationwide split on whether that Act bars civil RICO claims, and will engender confusion and uncertainty over the correct role federal law has regarding regulation of the business of insurance.

DATED: September 1, 1995.

CROSBY, HEAFEY, ROACH & MAY
Professional Corporation

By _____
James C. Martin
Attorneys for Petitioners

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

MERCHANTS HOME DELIVERY SERVICE, INC., a California corporation,
Plaintiff,
vs.
RELIANCE GROUP HOLDINGS, INC., a Delaware corporation, et al.,
Defendants.

No. CV-92-6889-WMB

ORDER

I. BACKGROUND

Plaintiff Merchants Home Delivery Service ("MHDS") asserts that, through an elaborate scheme, the defendants defrauded them of insurance premiums either through overcharging MHDS for the insurance coverage that was obtained for it or by never obtaining insurance coverage that was prepaid. The Amended Complaint alleges that a group of individual defendants conspired together to defraud the plaintiff and others. It also alleges that the individual defendants used the firms they worked at to facilitate the fraudulent scheme. Some of these firms and their successors in interest are the Prometheus defendants who have brought this motion for a judgment on the pleadings.[1] Two of the

[1] The defendants included as the Prometheus Defendants are: PROMETHEUS FUNDING CORP., (erroneously named as "Prometheus Liquidating Corp." and successor to the now defunct named defendant "FRANK B. HALL & CO., INC." a Delaware corporation), FRANK B. HALL INSURANCE BROKERS, INC., a New York corporation, (formerly dba FRANK B. HALL & CO. OF CALIFORNIA INSUR-

defendants are or were under criminal indictment for fraudulent activities.[2]

Plaintiff originally alleged nine causes of action against the defendants. The first two claims alleged violations of civil RICO. 18 U.S.C. § 1962(c)-(d). The remaining seven causes of action were pendent state claims which the Court dismissed without prejudice in April, 1993.

The Prometheus defendants bring this motion for a judgment on the pleadings pursuant to section 12(c) of the Federal Rules of Civil Procedure. Defendants allege that the remaining two RICO claims are barred by the provisions of the McCarran-Ferguson Act, 15 U.S.C. § 1012(b).

II. DISCUSSION

A. Standard

Under Fed. R. Civ. P. 12(c), a party is entitled to a judgment on the pleadings where no issues of material fact exist and the moving party is entitled to a judgment as a matter of law. It is almost identical to a 12(b)(6) motion for failure to state a claim, in that the Court is to view the facts presented in the pleadings "in the light most favorable to the plaintiffs, accepting as true all of the allegations in their complaint and treating as false those allegations in the answer that contradict the plaintiffs' allegations." *Hoeft v.*

ANCE BROKERS, a division of FRANK B. HALL INSURANCE BROKERS, INC., and "FRANK B. HALL & CO." and FRANK B. HALL & CO. OF CALIFORNIA, dba "BALDEN, CARTER & VILES" and "FLETCHER, LAWRENCE, PRUETER & DODDS"), AON CORPORATION, ROLLINS HUDIG HALL and ROLLINS HUDIG HALL OF SOUTHERN CALIFORNIA, INC.

[2]One of the defendants under indictment, Ismay, entered into a plea of guilty and was sentenced to 4 years confinement. The other defendant, Smalridge, based upon the last information presented to the Court, was scheduled for trial in early July.

Tucson Unified School Dist., 967 F.2d 1298, 1301 n.2 (9th Cir. 1992).

The Court should not grant a judgment under Rule 12(c) unless "it is clear that the merits of the controversy can be fairly and fully decided in this summary manner." 5A C. Wright & A. Miller, *Federal Practice and Procedure*, § 1369, at 534-535 (1990 and 1992 Supp.).

B. Whether the McCarran-Ferguson Act Bars MHDS's RICO Claims

The McCarran-Ferguson Act was passed by Congress in 1945 to statutorily reverse *United States v. South-Eastern Underwriters Association*, 64 S.Ct. 1162 (1944), which held that the business of insurance was subject to all federal laws. The McCarran-Ferguson Act states:

> No Act of congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance.

15 U.S.C. § 1012(b). The Congressional purpose behind the Act was to give states primary jurisdiction over the regulation of the business of insurance. *Cochran v. Paco, Inc.*, 606 F.2d 460, 463 (5th Cir. 1979).

The Fifth Circuit case of *Cochran v. Paco, Inc., supra*, establishes the test used to determine the applicability of the McCarran-Ferguson Act. *Cochran* held that the McCarran-Ferguson Act bars the application of a federal statute where:

(1) the federal statute does not relate specifically [to] the business of insurance;

(2) the complained of activities constitute the business of insurance;

(3) the state has enacted laws for the purpose of regulating the complained of activity; and

(4) the application of the federal statute would invalidate, impair or supersede state legislation.

Cochran, 606 F.2d at 464 (adopting analysis of *Securities & Exchange Comm'n v. National Securities, Inc.*, 89 S.Ct. 564, 567-569 (1969)); *see also LeDuc v. Kentucky Central Life Insurance Company*, 814 F. Supp. 820, 826-27 (NB.D. Cal. 1992) (citing *Cochran*); *American International Group, Inc. v. Superior Court*, 285 Cal. Rptr. 765 (1991) (same).

1. Whether RICO specifically relates to the business of insurance

The point is not disputed. RICO clearly does not specifically address the business of insurance.

2. Whether the conduct in the complaint constitutes the business of insurance

The interpretation of what constitutes the "business of insurance" is a federal question and the "federal interpretations supersede those of state courts." *Securities & Exchange Comm'n v. Variable Annuity Life Ins. Co.*, 79 S.Ct. 618, 621 (1959). The United States Supreme Court has stated that the marketing, advertising, sale and performance of insurance policies constitutes the "business of insurance." *FTC v. National Casualty Co.*, 78 S.Ct. 1260 (1958).

The Supreme Court has listed three elements to be considered in determining whether activity constitutes the business of insurance; (1) whether the practice has the effect of transferring or spreading a policyholder's risk; (2) whether the practice is an integral part of the policy relationship between the insurer and the insured; and (3) whether the practice is limited to entities within the insurance industry. *Group Life & Health Ins. Co. v. Royal Drug Co.*, 99 S.Ct. 1067 (1979). These factors are not binding: "no one is dispositive, rather each is instructive." *United*

Food & Commercial Workers v. Pacyga, 801 F.2d 1157, 1161 (9th Cir. 1986).

MHDS argues that the practices alleged in this case fall into two categories. The first category asserted is soliciting and obtaining "insurance premium" payments from MHDS for nonexistent, fictitious policies and pocketing the money.[3] The second category asserted is overcharging MHDS on real, existing insurance policies, and pocketing the difference between the true premium amount and the amount charged.[4] MHDS argues that these activities do not satisfy the factors set out in *Royal Drug* and therefore do not constitute engaging in the business of insurance.

MHDS did not separate its allegations against the defendants into these two neat categories until recently when it did so in its attempt to circumvent the McCarran-Ferguson Act. MHDS's Amended Complaint alleges that the defendants "conceived the idea of using their insurance brokerage business . . . as a platform from which to swindle and bilk their insurance customers of premium payments . . ." (Amended Complt. p. 12) and then convinced MHDS to switch all of its insurance programs and business to the defendants. (*Id.* at 14). MHDS alleges that, in 1986, defendants made a proposal to provide insurance services to MHDS and that MHDS accepted this insurance proposal (*Id.*). The Amended Complaint also alleges that for each successive year, defendants made insurance renewal proposals which MHDS accepted. (*Id.* at 15).

In addition, the amended Complaint asserts that defendants instituted a pass-through procedure so the billing and invoicing for MHDS's insurance premiums would go di-

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[3]MHDS alleges that the amount it was defrauded through this activity was at least $979,493.

[4]MHDS alleges that the amount it was defrauded through this activity was at least $309,421.

rectly to the defendants from the other insurance carriers. (*Id.* at 16). MHDS claims this was done so that defendants could misrepresent premiums, overbill for insurance coverage, bill for insurance coverage not provided, set excess estimated premiums, misrepresent the amount and/or validity of the claims, and retain funds due to MHDS. (*Id.* at 17).

It is clear that the actual allegations contained in the Amended Complaint assert more than just two simple categories of fraud. Rather, the allegations assert a broad scheme in which the defendants committed fraud within the insurance industry. Therefore, an analysis of the *Royal Drug* factors are not necessary since the allegations against the defendants fall squarely within the definition of marketing and sale of insurance policies. However, as an alternative basis, the Court provides an analysis of the *Royal Drug* factors.

a. Whether the practice has the effect of transferring or spreading a policyholder's risk

The Ninth Circuit has characterized the transferring or spreading of a policyholder's risk as "the primary characteristic of the business of insurance." *Feinstein v. Nettleship Co. of Los Angeles*, 714 F.2d 928, 931 (9th Cir. 1983).

MHDS argues that neither of the activities that it alleges defendants participated in operate to spread policyholders' risk. MHDS asserts that the transfer of risk is "effected by means of the contract between the parties — the insurance policy — and that transfer is complete at the time that the contract is entered." *Union Labor Life Ins. Co. v. Pireno*, 102 S.Ct. 3002, 3009 (1982). Here, MHDS contends, the parties never entered a contract with regard to the first category of fraud because defendants took the money and never gave MHDS the policy. As for the second category, MHDS argues that the defendants overcharging it for the

premiums is unconnected to the transfer of risk accomplished when the contract was entered.

The Court disagrees with MHDS. MHDS alleges in its Amended Complaint that defendants, as insurance brokers, made policy renewal proposals, billed and invoiced MHDS for the insurance policy premiums and accepted the insurance premiums. These are classic activities in the insurance industry that operate to spread the risk. Moreover, the payment of the insurance premiums in return for policies, even if overpriced as alleged, still is a practice that effectuates the transfer of risk.

b. Whether the practice is an integral part of the policy relationship between the insurer and the insured

MHDS argues that a broker taking money and giving nothing in return or a broker overcharging for coverage can never be considered an integral part of the insurer-insured relationship. In addition, MHDS asserts that, as brokers, the defendants are not insurers and therefore are not an integral part of the insurance relationship. Finally, MHDS asserts that it was a victim, not an insured, because the premiums paid did not yield an insurance policy. Therefore, MHDS asserts, there is no insurer-insured relationship present in this case.

Under California Insurance Code § 33, an insurance broker in California transacts insurance. Brokers are the middlemen and, as such, they form an integral part of the insurance relationship. It is alleged that the defendants made insurance policy renewal proposals, billed and invoiced MHDS for the policy premiums, and accepted the premiums. As pointed out by the defendants, the broker markets, advertises and sells policies for the insurer, negotiates coverage and obtains policies for the insured, and accepts premiums. This satisfies the McCarran-Ferguson

Act requirement that the broker be involved in the business of insurance.

c. Whether the practice is limited to entities within the insurance industry

MHDS asserts that the case fails this prong because the type of fraud engaged in by defendants is not limited to the insurance industry. MHDS argues that the fraud in this case is the same as a real estate scheme where a broker receives money and does not provide any property in return. The fact that it is insurance policies, MHDS contends, is tangential and does not operate to satisfy this prong of the *Royal Drug* test.

Once again, MHDS is attempting to read its Amended Complaint more narrowly than it is written. The Amended Complaint alleges the defendants were brokers who made insurance policy renewal proposals, obtained the renewals, and accepted the insurance premiums. These alleged activities are by definition limited to the insurance industry.

d. Conflict in the district courts

There are two competing cases in the California district courts that directly address whether insurance-related activities involving fraud fall within the business of insurance.

In *LeDuc v. Kentucky Central Life Insurance Co.*, 814 F.Supp. 820 (N.D. Cal. 1992), the district court examined insurance agents' claims that the insurance company they represented engaged in fraudulent practices to induce agents to sell more insurance and investments at higher premiums. The court held that the McCarran-Ferguson Act barred the insurance agents' claims because the insurer's "alleged fraudulent activity is . . . within the business of insurance because it is directed at the purchasing public and is intended to induce the purchase of insurance." *LeDuc*, 814 F.Supp. at 827.

The court in *Thacker v. New York Life Insurance Co.*, 796 F.Supp. 1338, 1342 (E.D. Cal. 1992), found that insurance-related activity was not within the "business of insurance" when the activity involved fraud. The court reasoned that the person committing the fraud could "hardly be heard to assert that mail fraud is the ordinary business of insurance." *Thacker*, 796 F.Supp. at 1342.

The Court finds the *LeDuc* reasoning more persuasive. If courts followed the *Thacker* analysis, the McCarran-Ferguson Act would never act to bar a federal statute because the wrongdoing would always be outside the ordinary course of the business of insurance. This would subvert the policy behind the McCarran-Ferguson Act which was to allow states to regulate the insurance industries.

3. Whether California has enacted laws for the purpose of regulating the type of activity complained of in this case

California has a statute that was passed in direct response to the McCarran-Ferguson Act. California Insurance Code § 790 states:

> The purpose of this article is to regulate trade practices in the business of insurance in accordance with the intent of Congress as expressed in the [McCarran-Ferguson Act], by defining, or providing for the determination of, all such practices in this State which constitute unfair methods of competition or unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined.

This Act applies to brokers. Cal. Ins. Code § 790.01.

MHDS argues that this Act is not applicable because it does not purport to regulate misrepresentations about the very existence of insurance policies. The Court rejects this argument. Section 790 regulates all trade practices in the

business of insurance. Specifically, the Act prohibits the making of any misrepresentation "regarding the terms of any policy issued or to be issued or the benefits or advantages promised thereby." Cal. Ins. Code § 790.03. The First Amended Complaint alleges that defendants accepted premiums for policies and coverage that MHDS did not receive. If MHDS thought it was supposed to receive a policy or certain coverage by way of a policy, the logical implication is that it was because it was told something false about the policies by the defendants. This type of misrepresentation is directly regulated by the Insurance Code.

4. Whether the application of RICO would invalidate, impair or supersede state legislation

RICO contains provisions for treble damages and attorneys' fees, neither of which is allowed under the California statutory scheme. Therefore, RICO would not just provide "parallel" remedies as asserted by MHDS. It would supersede the state remedies.

III. CONCLUSION

The Prometheus defendants' motion for judgment on the pleadings is granted. The RICO causes of action are barred by the McCarran-Ferguson Act: (1) RICO is not a federal insurance statute; (2) the defendants are alleged to have acted in the business of insurance; (3) California has a comprehensive statutory scheme covering the alleged conduct; and (4) allowing RICO to operate would supersede the state statutory scheme. If MHDS wants to pursue its claims against the defendants, it should do so in state court.

DATED: July 24, 1993.

Wm. Matthew Byrne, Jr.
United States District Judge

NOT FOR PUBLICATION
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

Filed
June-8 1995
Cathy A. Catterson, Clerk
U.S. Court of Appeals

MERCHANTS HOME DELIVERY SERVICE, INC., a California corporation,
Plaintiff-Appellant,
v.
FRANK B. HALL & CO., INC., a Delaware corporation; PROMETHEUS LIQUIDATING CORP., a Delaware corp.; FRANK B. HALL INSURANCE BROKERS, INC., a Delaware corp.; JAMES DWIGHT ISMAY, an individual; TERRY DON SMALRIDGE, an individual; PAUL C. CARTER, an individual,
Defendants-Appellees.

No. 93-56302
D.C. No.
CV-92-06889-WMB

MERCHANTS HOME DELIVERY SERVICE, INC., a California corporation,
Plaintiff-Appellant,

v.

FRANK B. HALL & CO., INC., a Delaware corporation; PROMETHEUS LIQUIDATING CORP., a Delaware corporation; FRANK B. HALL INSURANCE BROKERS, INC., a Delaware corporation,
Defendants,

and

PAUL C. CARTER, an individual,
Defendant-Appellee.

No. 93-56589

D.C. No. CV-92-06889-WMB (V)

MERCHANTS HOME DELIVERY SERVICE, INC., a California corporation,
Plaintiff-Appellant,
v.
FRANK B. HALL & CO., INC., a Delaware corporation; PROMETHEUS LIQUIDATING CORP., a Delaware corp.; FRANK B. HALL INSURANCE BROKERS, INC., a Delaware corp.; JAMES DWIGHT ISMAY, an individual; TERRY DON SMALRIDGE, an individual,
Defendants-Appellees,
and
PAUL C. CARTER, an individual,
Defendant.

No. 94-55035
D.C. No.
CV-92-06889-WMB(T)

ORDER

Before: BROWNING, BOOCHEVER and BEEZER, Circuit Judges.

The panel has voted unanimously to deny the petition for rehearing. Judges Browning and Beezer vote to reject the suggestion for rehearing en banc and Judge Boochever so recommends.

The full court has been advised of the suggestion for rehearing en banc and no judge in active service has requested a vote to rehear the matter en banc. Fed. R. App. P. 35.

The petition for rehearing is DENIED and the suggestion for rehearing en banc is REJECTED.

COURT OF APPEALS OPINION

MERCHANTS HOME DELIVERY SERVICE, INC.,
a California corporation,
Plaintiff-Appellant,

vs.

FRANK B. HALL & CO., INC., a Delaware corporation;
PROMETHEUS LIQUIDATING CORP., a Delaware corp.;
FRANK B. HALL INSURANCE BROKERS, INC., a Delaware corp.; JAMES DWIGHT ISMAY, an individual;
TERRY DON SMALRIDGE, an individual;
PAUL C. CARTER, an individual,
Defendants-Appellees,

MERCHANTS HOME DELIVERY SERVICE, INC.,
a California corporation,
Plaintiff-Appellant,

vs.

FRANK B. HALL & CO., INC., a Delaware corp;
PROMETHEUS LIQUIDATING CORP., a Delaware corp.;
FRANK B. HALL INSURANCE BROKERS, INC.,
a Delaware corporation,
Defendants,

and

PAUL C. CARTER, an individual,
Defendant-Appellee.

MERCHANTS HOME DELIVERY SERVICE, INC.,
a California corporation,
Plaintiff-Appellant,

vs.

FRANK B. HALL & CO., INC., a Delaware corporation;
PROMETHEUS LIQUIDATING CORP., a Delaware corp.;
FRANK B. HALL INSURANCE BROKERS, INC.,
a Delaware corp.;

JAMES DWIGHT ISMAY, an individual;
TERRY DON SMALRIDGE, an individual,
Defendants-Appellees,

and

PAUL C. CARTER, an individual,
Defendant.
Nos. 93-56302, 93-56589, 94-55035.

United States Court of Appeals, Ninth Circuit,
Argued and Submitted, March 8, 1995
Decided March 28, 1995.

Before: BROWNING, BOOCHEVER and BEEZER, Circuit Judges.

BEEZER, Circuit Judge:

Plaintiff Merchants Home Delivery Service, Inc. ("Merchants") appeals the district court's judgments dismissing Merchants' action against its former insurance broker, Frank B. Hall & Co., Inc. and associated defendants (collectively "Hall"). Merchants' complaint asserts claims under the Racketeer Influenced and Corrupt Organizations Act ("RICO"). See 18 U.S.C. §§ 1961-1968. The district court granted Hall's motion for judgment on the pleadings due to the court's determination that section 2(b) of the McCarran-Ferguson Act (15 U.S.C. § 1011, et seq.) precluded the application of RICO to Hall's alleged wrongdoing. We have jurisdiction pursuant to 28 U.S.C. § 1291. We reverse and remand.

I

Merchants' complaint alleges: Merchants is a national company engaged in shipping and delivering packages. It retained Hall on a continuing basis to secure numerous insurance policies and to process claims for which Merchants was self-insured. Merchants says that employees

of Hall, with Hall's knowledge or acquiescence, defrauded Merchants in three ways: (1) by overbilling Merchants for insurance premiums on actual policies, (2) by billing Merchants for premiums on nonexistent policies, and (3) by billing Merchants for direct, uninsured claims that were never paid to the claimants. Merchants alleges that these fraudulent acts were accomplished through use of the mails and wires, thus bringing them within the scope of RICO.

Merchants asserts numerous state law claims in addition to its RICO claims. The district court declined to exercise supplemental jurisdiction over the state law claims, and Merchants is pursuing those claims in state court. Hall moved for judgment on the pleadings (Fed. R. Civ. P. 12(c)), which the district court granted, ultimately disposing of the claims against all defendants in three successive judgments. Merchants timely appealed from each judgment and the appeals were consolidated.

II

We review a judgment on the pleadings *de novo*, *Westlands Water Dist. v. Firebaugh Canal*, 10 F.3d 667, 670 (9th Cir. 1993). Judgment on the pleadings is properly granted when, taking all allegations in the pleadings as true, the moving party is entitled to judgment as a matter of law. *Id.* The district court determined that, irrespective of whether Merchants' complaint states a claim under RICO, judgment in favor of Hall was appropriate because the operation of the McCarran-Ferguson Act makes RICO inapplicable to the facts alleged.

III

Congress enacted the McCarran-Ferguson Act in part to allow the states to regulate the business of insurance free from inadvertent preemption by federal statutes of general

applicability. *See Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 218, 99 S.Ct. 1067, 1076, 59 L. Ed. 2d 261 (1979). Section 2(b) of the Act accomplishes this purpose through a limited "inverse preemption," by directing that a federal law of general applicability does not apply to the "business of insurance" if the federal law conflicts with state laws enacted to regulate that business. *See* 15 U.S.C. § 1012(b).

Section 2(b) provides, in relevant part: "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance." *Id.* The terms of the statute suggest a four part inquiry for determining when § 2(b) precludes the application of a federal statute. *See Cochran v. Paco, Inc.*, 606 F.2d 460, 464 (5th Cir. 1979). The McCarran-Ferguson Act precludes the application of a federal statute if: (1) the statute does not "specifically relate" to the business of insurance, (2) the acts challenged under the statute constitute the business of insurance, (3) the state has enacted a law or laws regulating the challenged acts, and (4) the state law would be superseded, impaired or invalidated by the application of the federal statute. *Id.* All four factors must be satisfied. The parties agree that this well-settled four factor test governs the present dispute.

The first and third elements are not at issue here. As Merchants concedes, RICO does not specifically relate to the business of insurance. *See* 18 U.S.C. §§ 1961, 1962 (listing activities proscribed by RICO). Also, California has enacted a comprehensive insurance code, which prohibits the acts alleged by Merchants.[1] *See Feinstein v. Nettle-*

[1]Merchants argues that certain of Hall's alleged practices are not regulated by the California Insurance Code *because the practices are not*

ship Co., 714 F.2d 928, 933 (9th Cir. 1983), *cert. denied*, 466 U.S. 972, 104 S. Ct. 2346, 80 L. Ed. 2d 820 (1984); Cal. Ins. Code §§ 790-790.10 (West 1995). Thus, only the second and fourth elements are disputed.

IV

We first address whether the practices alleged by Merchants fall within the business of insurance under § 2(b). We hold that overcharging for premiums on actual insurance policies is the business of insurance, but that collecting premiums on false policies and charging for unpaid, uninsured claims are not.

A

The parties contest the proper scope of inquiry concerning whether the acts challenged under RICO constitute the business of insurance. Merchants argues that the court must look only to the wrongful component of the acts alleged, positing that "fraud and theft cannot be the 'business of insurance.'" It finds support for this position in several district court decisions. *See, e.g., Thacker v. New York Life Ins. Co.*, 796 F. Supp. 1338, 1342 (E.D. Cal. 1992). Hall argues that this approach is much too narrow, and that the entire relationship between the parties must be examined to determine whether the challenged acts occurred in the business of insurance. Hall's position also has support from several district courts. *See, e.g., Wexco, Inc. v. IMC, Inc.*, 820 F. Supp. 194, 199 (M.D. Pa. 1993). The district court adopted Hall's reasoning.

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the business of insurance. This is simply a repetition of Merchants' argument on the second element. The relevant inquiry on the third element is satisfied; to the extent Hall's acts *do* constitute the business of insurance, it is not disputed that the acts are proscribed by the California Insurance Code.

Neither party has identified the proper scope of inquiry. The approach put forth by Hall is too broad. The Supreme Court has stated that the McCarran-Ferguson Act "does not exempt the business of insurance companies .... The exemption is for the 'business of insurance[.]' " *Royal Drug,* 440 U.S. at 210-11, 99 St. Ct. at 1073. Thus, the proper inquiry is whether a particular "practice constitutes the business of insurance," not whether the defendant or the plaintiff transact the business of insurance in general. *See Nettleship,* 714 F. 2d at 931.

Merchants' proposed test, however, defines the challenged practice too narrowly. As the Seventh Circuit stated, "it is not helpful to point to a practice forbidden by federal law ... and observe that this practice is not itself insurance." *NAACP. v. American Family Mut. Ins. Co.*, 978 F.2d 287, 294 (7th Cir. 1992) (Easterbrook, J.) *cert. denied,* ____ U.S. ____, 113, S. Ct. 2335, 124 L. Ed. 2d 247 (1993). This interpretation of the rule would read the McCarran-Ferguson Act out of existence. Any practice which violated any federal statute would, by definition, not be the "business of insurance," resulting in all federal statutes applying to the business of insurance with their "full rigor." *See id.* This is not the result Congress intended. Therefore, we hold that the property inquiry is whether, taken as a whole, the specific practice being challenged under federal law is a part of the "business of insurance."

B

The Supreme Court has identified three factors to be applied in determining whether a practice constitutes the business of insurance: (1) whether the practice has the effect of transferring or spreading the policyholders' risks, (2) whether the practice is an integral part of the policy relationship between the insurer and the insured, and (3) whether the practice is limited to entities within the insur-

ance industry.[2] *See United Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129, 102 S. Ct. 3002, 3008-09, 73 L. Ed. 2d 647 (1982). The Supreme Court has made it clear that the transfer or spreading of the risk is the primary or even "indispensable" characteristic of the business of insurance. *Id.* at 127, 102 S. Ct. at 3007-08; *Royal Drug*, 440 U.S. at 211-12, 99 S. Ct. at 1073-74. Our own cases applying these factors also "emphasize that the primary characteristic of the business of insurance is the transferring or spreading of risk." *Nettleship*, 714 F.2d at 931.

Merchants alleges three types of fraudulent practices by Hall: (1) overcharging for premiums on actual policies, (2) collecting premiums on fictitious policies, and (3) collecting payments for uninsured claims which Hall did not actual pay. We address each practice separately.

I

Overcharging for premiums on actual policies is part of the business of insurance. All three factors are satisfied. First, Merchants actually was a party to an insurance policy which transferred and spread its risks. The payment and collection of premiums is necessary to the risk-spreading transaction; if the premiums are not paid, the policy will

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[2]Hall argues that this three factor analysis should only be applied in the antitrust area, where the "business of insurance" is meant to be defined narrowly. Hall contends that *United States Department of the Treasury v. Fabe*, ____ U.S. ____, 113 S. Ct. 2202, 124 L. Ed. 2d 449 (1993) supports this position. We disagree. *In Fabe*, the Supreme Court actually applied the three factors above, emphasizing that the acts involved there affected the transfer or spreading of risk. *See id.* at ____, 113 S. Ct. at 2208-09. On the other hand, Hall is correct that the Court held the business of insurance was to be defined more broadly outside the antitrust area. *Id.* at ____-____, 113 S. Ct. at 2209-10. This is a matter of degree, however, rather than a wholesale change in the inquiry.

lapse and the risk spreading relationship will be terminated. Second, an insurance broker's collection of premiums is integral, though not indispensable, to the relationship between the insured and the insurer. Finally, only in the insurance industry are insurance policies written and insurance premiums collected. Merchants' claim here is not that it was never insured or that its risk was not spread, but simply that it was charged more than it should have been for the insurance coverage it received. This type of transaction is at the core of the "business of insurance."

2

We fail to see, however, how the collection of premium payments for nonexistent policies falls within the business of insurance. Where there is no insurance policy, the first two factors are not satisfied: Merchants' risk is not spread, and there is no relationship at all between it and the insurer. This conclusion is supported by the very wording of the first two factors, which assumes the existence of a "policy." *See Nettleship*, 714 F.2d at 931 (explaining that inquiries are whether the "policyholder's" risk is spread, and whether the practice is an integral part of the "policy relationship between insurer and insured"). The third factor is arguably not satisfied either. Because no policy was sold at all, this practice comes close to being the "business of fraud," as characterized by Merchants. Money can be fraudulently collected for a nonexistent product in any field. On the other hand, where the products falsely being offered are insurance policies, public policy concerns specific to the business of insurance may be implicated (e.g. there may be a particularly strong public interest concern against such fraud, as it directly affects the existence and reliability of insurance contracts). Therefore, the third factor does not weigh conclusively in either direction.

Given the Supreme Court's clear statements that the transfer or spreading of risk is the primary factor to be considered, the absence of this element requires, at a minimum, that the other two factors weigh strongly in Hall's favor in order for its practice to fall within the business of insurance. *See SEC v. National Sec., Inc.*, 393 U.S. 453, 460, 89 S.Ct. 564, 568, 21 L.Ed.2d 668 (1969) ("The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation and enforcement — these were the core of the 'business of insurance.' ") The existence of a contractual policy relationship is therefore of central, if not essential, importance. Hall has not shown that the practice of collecting premiums on sham insurance policies "relate[s] so closely" to the policy relationship as to outweigh the lack of a policy itself. *See, id.*

3

The third challenged practice, collecting money for false claims to be directly paid by Merchants, is not even arguably the business of insurance. This practice satisfies none of the factors. There is no spreading or transfer of the risk. Indeed, even had the transactions not been fraudulent, the parties always contemplated that Merchants would bear its own risk. There is no policy relationship between Merchants and any insurer. Finally, the practice is not limited to the insurance industry. Merchants could pay these claims itself, without using Hall as an intermediary, or could use a different company as its agent for claims adjustment. Hall simply happens to be an insurance broker which Merchants engaged to administer claims settlement. This practice is not the business of insurance.

V

As some of Hall's alleged practices fall within the business of insurance, it is necessary for us to determine whether

the application of RICO to those practices would "invalidate, impair, or supersede" California's laws regulating those practices. We hold the application of RICO to Hall's alleged fraudulent acts is consistent with California's insurance laws.

A

The parties again argue in favor of widely disparate standards for determining whether a federal law invalidates, impairs or supersedes state insurance regulations. Hall argues that the term "impair" is intended to be a very broad proscription against applying federal law where a state has regulated, *or chosen not to regulate*, in the insurance industry. Under this construction of § 2(b), Hall argues that the private right of action for treble damages and mandatory attorney fees allowed by RICO would upset the balance struck by California's insurance code, which, in general, allows only administrative enforcement and actual damages. *See Moradi-Shalal v. Fireman's Fund Ins. Cos.*, 46 Cal. 3d 287, 250 Cal. Rptr. 116, 758 P.2d 58, 68-69 (1988). Again, Hall draws on district court decisions to support its position. *See, e.g., Wexco*, 820 F. Supp. at 204. This argument amounts to the contention that Congress intended the McCarran-Ferguson Act to allow states to preempt the field in the regulation of the business of insurance.

Merchants counters with a much narrower reading of the McCarran-Ferguson Act's "inverse preemption." Under Merchants' construction, application of a federal law would be precluded only where the federal law expressly prohibited acts permitted by state law, or vice versa. Further, Merchants' argues that the California statute's express statement that it is cumulative with *state* common law causes of action weighs against Hall's "delicate balance" argument. Merchants has support from several district

courts for this position as well. *See, e.g., Thacker,* 796 F. Supp. at 1343.

We have not previously addressed the question of exactly when a federal statute "invalidate[s], impair[s], or supersede[s]" a state law under § 2(b). The Seventh Circuit, however, recently addressed this issue in *NAACP v. American Family Mutual Insurance Co.,* 978 F.2d 287 (7th Cir. 1992). In that case, the court was faced with the question of whether the Fair Housing Act could be invoked to prohibit "redlining" by home insurers. As in the present case, state law prohibited the conduct, but allowed only administrative remedies, whereas the federal law allowed a private right of action. *See id.* at 295. In a very thorough opinion, Judge Easterbrook expressly rejected the "upset the balance" argument and concluded that the narrower "direct conflict" construction of the McCarran-Ferguson Act was appropriate. *Id.* at 296-97.

In reaching its conclusion, the Seventh circuit analogized to the principles governing *federal* preemption of *state* law in areas heavily regulated by federal statute. For example, in the area of nuclear power, despite pervasive federal regulation and a lower cap on liability under federal law, the Supreme Court upheld a state punitive damages award for acts prohibited by both state and federal law. *See Silkwood v. Kerr-McGee Corp.,* 464 U.S. 238, 256, 104 S.Ct. 615, 624, 78 L.Ed.2d 443 (1984). The Seventh Circuit went on to catalog many additional Supreme Court cases upholding cumulative state *remedies* for conduct deemed wrongful under both state and federal law. *American Family,* 978 F.2d at 2963[3] Thus, the court concluded that state and federal laws proscribing identical conduct do not con-

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[3] Although *Silkwood's* specific holding was superseded by statute (42 U.S.C. § 2210(s)), the general principle remains viable.

flict with or displace each other, and may coexist under the McCarran-Ferguson Act. *Id.* at 297.

We adopt the Seventh Circuit's well-reasoned approach. The language of § 2(b) is inconsistent with a congressional intent to allow states to preempt the field of insurance regulation. First, § 2(b)'s exemption of federal laws which specifically relate to the business of insurance weighs against a congressional intent wholly to abandon the field to the states. Second, only federal statutes which "invalidate, impair, or supersede" state insurance statutes are "preempted." If Congress had intended to cede the field, it could have said: "No federal statute shall be construed to *apply* to the business of insurance." Instead, it allowed federal statutes to apply unless they conflict with the states' statutes. The terms of the Act's "inverse preemption" are not so broad as Hall would have it.

We hold that the application of a federal statute prohibiting acts which are also prohibited under a state's insurance laws does not "invalidate, impair, or supersede" the state's laws under § 2(b) of the McCarran-Ferguson Act.

B

Under this rule, § 2(b) allows the application of RICO to the present facts. Hall concedes, indeed strenuously argues, that California law prohibits the acts alleged by Merchants. As RICO prohibits these same acts, there is no conflict; RICO does not invalidate, impair, or supersede California law in this context.

VI

We REVERSE the district court's judgments in favor of defendants and REMAND to that court for further proceedings consistent with this opinion.

18 U.S.C. § 1964. Civil Remedies

(a) The district courts of the United States shall have jurisdiction to prevent and restrain violations of section 1962 of this chapter by issuing appropriate orders, including, but not limited to: ordering any person to divest himself of any interest, direct or indirect, in any enterprise; imposing reasonable restrictions on the future activities or investments of any person, including but not limited to, prohibiting any person from engaging in the same type of endeavor as the enterprise engaged in, the activities of which affect interstate or foreign commerce; or ordering dissolution or reorganization of any enterprise, making due provision for the rights of innocent persons.

(b) The Attorney General may institute proceedings under this section. Pending final determination thereof, the court may at any time enter such restraining orders or prohibitions, or take such other actions, including the acceptance of satisfactory performance bonds, as it shall deem proper.

(c) Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee.

(d) A final judgment or decree rendered in favor of the United States in any criminal proceeding brought by the United States under this chapter shall estop the defendant from denying the essential allegations of the criminal offense in any subsequent civil proceeding brought by the United States.

CALIFORNIA'S UNFAIR INSURANCE PRACTICES ACT

California Insurance Code § 790 Purpose Of Article; Regulation Of Trade Practices In Insurance Business

The purpose of this article is to regulate trade practices in the business of insurance in accordance with the intent of Congress as expressed in the Act of Congress of March 9, 1945 (Public Law 15, Seventy-ninth Congress),[4] by defining, or providing for the determination of, all such practices in this State which constitute unfair methods of competition or unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined.

§ 790.01. Application Of Article

This article applies to reciprocal and interinsurance exchanges, Lloyds insurers, fraternal benefit societies, fraternal fire insurers, grants and annuities societies, insurers holding certificates of exemptions, motor clubs, non-profit hospital associations, life agents, broker-agents, surplus line brokers and special lines surplus line brokers as well as all other persons engaged in the business of insurance.

§ 790.02. Engaging In Trade Practice Defined As Unfair Method Of Competition Prohibited

No person shall engage in this State in any trade practice which is defined in this article as, or determined pursuant to this article to be, an unfair method of competition or an unfair or deceptive act or practice in the business of insurance.

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[4] 15 U.S.C.A. §§ 1011 *et seq.*

§ 790.03. Prohibited Acts

The following are hereby defined as unfair methods of competition and unfair and deceptive acts or practices in the business of insurance.

(a) *[Misrepresentations: False or Misleading Statements]* Making, issuing, circulating, or causing to be made, issued or circulated, any estimate, illustration, circular or statement misrepresenting the terms of any policy issued or to be issued or the benefits or advantages promised thereby or the dividends or share of the surplus to be received thereon, or making any false or misleading statement as to the dividends or share of surplus previously paid on similar policies, or making any misleading representation or any misrepresentation as to the financial condition of any insurer, or as to the legal reserve system upon which any life insurer operates, or using any name or title of any policy or class of policies misrepresenting the true nature thereof, or making any misrepresentation to any policyholder insured in any company for the purpose of inducing or tending to induce such policyholder to lapse, forfeit, or surrender his or her insurance.

(b) *[Untruthful, Deceptive, or Misleading Statements]* Making or disseminating or causing to be made or disseminated before the public in this state, in any newspaper or other publication, or any advertising device, or by public outcry or proclamation, or in any other manner or means whatsoever, any statement containing any assertion, representation or statement with respect to the business of insurance or with respect to any person in the conduct of his or her insurance business, which is untrue, deceptive, or misleading, and which is known, or which by the exercise of reasonable care should be known, to be untrue, deceptive, or misleading.

(c) *[Unreasonable Restraint of, or Monopoly in, Business of Insurance]* Entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance.

(d) *[False Statements of Insurer's Financial Condition]* Filing with any supervisory or other public official, or making, publishing, disseminating, circulating, or delivering to any person, or placing before the public, or causing directly or indirectly, to be made, published, disseminated, circulated, delivered to any person, or placed before the public any false statement of financial condition of an insurer with intent to deceive.

(e) *[False Entries; Willful Omissions]* Making any false entry in any book, report, or statement of any insurer with intent to deceive any agent or examiner lawfully appointed to examine into its condition or into any of its affairs, or any public official to whom the insurer is required by law to report, or who has authority by law to examine into its condition or into any of its affairs, or, with like intent, willfully omitting to make a true entry of any material fact pertaining to the business of the insurer in any book report, or statement of the insurer.

(f) *[Unfair Rate Discrimination]* Making or permitting any unfair discrimination between individuals of the same class and equal expectation of life in the rates charged for any contract of life insurance or life annuity or in the dividends or other benefits payable thereon, or in any other of the terms and conditions of the contract.

This subdivision shall be interpreted, or any contract of ordinary life insurance or individual life annuity applied for and issued on or after January 1, 1981, to require differentials based upon the sex of the individual insured or annui-

tant in the rates or dividends or benefits, or any combination thereof. This requirement is satisfied if those differentials are substantially supported by valid pertinent data segregated by sex, including, but not necessarily limited to, mortality data segregated by sex.

However, for any contract of ordinary life insurance or individual life annuity applied for and issued on or after January 1, 1981, but before the compliance date, in lieu of those differentials based on data segregated by sex, rates, or dividends or benefits, or any combination thereof, for ordinary life insurance or individual life annuity on a female life may be calculated as follows: (a) according to an age not less than three years nor more than six years younger than the actual age of the female insured or female annuitant, in the case of a contract of ordinary life insurance with a face value greater than five thousand dollars ($5,000) or a contract of individual life annuity; and (b) according to an age not more than six years younger than the actual age of the female insured, in the case of a contract of ordinary life insurance with a face value of five thousand dollars ($5,000) or less. "Compliance date" as used in this paragraph shall mean the date or dates established as the operative date or dates by future amendments to this code directing and authorizing life insurers to use a mortality table containing mortality data segregated by sex for the calculation of adjusted premiums and present values for nonforfeiture benefits and valuation reserves as specified in Section 10163.5 and 10489.2 or successor sections.

Notwithstanding the provisions of this subdivision, sex based differentials in rates or dividends or benefits, or any combination thereof, shall not be required for (1) any contract of life insurance or life annuity issued pursuant to arrangements which may be considered terms, conditions, or privileges of employment as these terms are used in Title VII of the Civil Rights Act of 1964 (Public Law 88-352), as

amended, and (2) tax sheltered annuities for employees of public schools or of tax exempt organizations described in Section 501(c)(3) of the Internal Revenue Code.

(g) *[Statement of Membership in California Insurance Association]* Making or disseminating, or causing to be made or disseminated, before the public in this state, in any newspaper or other publication, or any other advertising device, or by public outcry or proclamation, or in any other manner or means whatever, whether directly or by implication, any statement that a named insurer, or named insurers, are members of the California Insurance Guarantee Association, or insured against insolvency as defined in Section 119.5. This subdivision shall not be interpreted to prohibit any activity of the California Insurance Guarantee Association or the commissioner authorized, directly or by implication, by Article 14.2 (commencing with Section 1063).

(h) *[Unfair Claims Settlement Practices]* Knowingly committing or performing with such frequency as to indicate a general business practice any of the following unfair claims settlement practices:

(1) Misrepresenting to claimants pertinent facts or insurance policy provisions relating to any coverages at issue.

(2) Failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies.

(3) Failing to adopt and implement reasonable standards for the prompt investigation and processing of claims arising under insurance policies.

(4) Failing to affirm or deny coverage of claims within a reasonable time after proof of loss requirements have been completed and submitted by the insured.

(5) Not attempting in good faith to effectuate prompt, fair, and equitable settlements of claims in which liability has become reasonably clear.

(6) Compelling insureds to institute litigation to recover amounts due under an insurance policy by offering substantially less than the amounts ultimately recovered in actions brought by the insureds, when the insureds have made claims for amounts reasonably similar to the amounts ultimately recovered.

(7) Attempting to settle a claim by an insured for less than the amount to which a reasonable man would have believed he was entitled by reference to written or printed advertising material accompanying or made part of an application.

(8) Attempting to settle claims on the basis of an application which was altered without notice to, or knowledge or consent of, the insured, his or her representative, agent, or broker.

(9) Failing, after payment of a claim, to inform insureds or beneficiaries, upon request by them, of the coverage under which payment has been made.

(10) Making known to insureds or claimants a practice of the insurer of appealing from arbitration awards in favor of insureds or claimants for the purpose of compelling them to accept settlements or compromises less than the amount awarded in arbitration.

(11) Delaying the investigation or payment of claims by requiring an insured, claimant, or the physician of either, to submit a preliminary claim report, and then requiring the subsequent submission of formal proof of loss forms, both of which submissions contain substantially the same information.

(12) Failing to settle claims promptly, where liability has become apparent, under one portion of the insurance policy coverage in order to influence settlements under other portions of the insurance policy coverage.

(13) Failing to provide promptly a reasonable explanation of the basis relied on in the insurance policy, in relation to the facts or applicable law, for the denial of a claim or for the offer of a compromise settlement.

(14) Directly advising a claimant not to obtain the services of an attorney.

(15) Misleading a claimant as to the applicable statute of limitations.

(16) Delaying the payment or provision of hospital, medical, or surgical benefits for services provided with respect to acquired immune deficiency syndrome or AIDS-related complex for more than 60 days after the insurer has received a claim for those benefits, where the delay in claim payment is for the purpose of investigating whether the condition preexisted the coverage. However, this 60-day period shall not include any time during which the insurer is awaiting a response for relevant medical information from a health care provider.

§ 790.034. Regulations; Settlement of Claims

Regulations adopted by the commissioner pursuant to this article which relate to the settlement of claims shall take into consideration settlement practices by classes of insurers.

§ 790.035. Unfair Competition and Unfair or Deceptive Acts or Practices; Civil Penalty

(a) Any person who engages in any unfair method of competition or any unfair or deceptive act or practice defined in Section 790.03 is liable to the state for a civil penalty to be fixed by the commissioner, not to exceed five

thousand dollars ($5,000) for each act, or, if the act or practice was willful, a civil penalty not to exceed ten thousand dollars ($10,000) for each act. The commissioner shall have the discretion to establish what constitutes an act. However, when the issuance, amendment, or servicing of a policy or endorsement is inadvertent, all of those acts shall be a single act for the purpose of this section.

(b) The penalty imposed by this section shall be imposed by and determined by the commissioner as provided by Section 790.05. The penalty imposed by this section is appealable by means of any remedy provided by Section 12940 or by Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code.

§ 790.036. Advertising of Insurance that will not be Sold

(a) It is an unfair and deceptive act or practice in the business of insurance for an insurer to advertise insurance that it will not sell.

(b) Nothing in this section shall be construed to prohibit any insurer from advertising insurance products for which it is licensed to sell in this state where the product is not available for sale so long as the unavailability is disclosed in the advertisement.

(c) A violation of this section is subject to the sanctions provided for by this article.

(d) An intentional violation of this section is a misdemeanor punishable by a fine not exceeding ten thousand dollars ($10,000).

(e) This section does not apply to any insurer that refuses to sell a policy of insurance on the basis of its underwriting guidelines.

(f) This section does not apply to advertisements by an insurer where the advertisements are broadcast and origi-

nate from outside this state. As used in this subdivision, "broadcast" includes electronic media, television, and radio. As used in this subdivision, "originate from outside this state" includes cable transmittal of programs broadcast by stations located outside California.

§ 790.04. Powers of Commissioner; Examinations and Investigations

The commissioner shall have power to examine and investigate into the affairs of every person engaged in the business of insurance in the State in order to determine whether such person has been or is engaged in any unfair method of competition or in any unfair or deceptive act or practice prohibited by Section 790.03 or determined pursuant to this article to be an unfair method of competition or an unfair or deceptive practice in the business of insurance. Such investigation may be conducted pursuant to Article 2 (commending at Section 11180) of Chapter 2, Part 1, Division 3, Title 2 of the Government Code.

§ 790.05. Order to Show Cause; Hearing; Cease and Desist Order; Review

Whenever the commissioner shall have reason to believe that such person has been engaged or is engaging in this state in any unfair method of competition or any unfair or deceptive act or practice defined in Section 790.03, and that a proceeding by the commissioner in respect thereto would be to the interest of the public, he or she shall issue and serve upon that person an order to show cause containing a statement of the charges in that respect, a statement of that person's potential liability under Section 790.035, and a notice of a hearing thereon to be held at a time and place fixed therein, which shall not be less than 30 days after the service thereof, for the purpose of determining whether the commissioner should issue an order to that person to, pay

the penalty imposed by Section 790.035, and to cease and desist those methods, acts, or practices or any of them.

If the charges or any of them are found to be justified the commissioner shall issue and cause to be served upon that person an order requiring that person to pay the penalty imposed by Section 790.035 and to cease and desist from engaging in those methods, acts, or practices found to be unfair or deceptive.

The hearing shall be conducted in accordance with the Administrative Procedure Act, Chapter 5 (commencing at Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code, and the commissioner shall have all the powers granted therein.

The person shall be entitled to have the proceedings and the order reviewed by means of any remedy provided by Section 12940 of this code or by the Administrative Procedure Act.

§ 790.06. Engaging in Practices Not Defined in Section 790.03

(a) Whenever the commissioner shall have reason to believe that any person engaged in the business of insurance is engaging in this State in any method of competition or in any act or practice in the conduct of such business which is not defined in Section 790.03 and that such method is unfair or that such act or practice is unfair or deceptive and that a proceeding by him in respect thereto would be in the interest of the public, he may issue and serve upon such person an order to show cause containing a statement of the methods, acts or practices alleged to be unfair or deceptive and a notice of hearing thereon to be held at a time and place fixed therein, which shall not be less than 30 days after the service thereof, for the purpose of determining whether the alleged methods, acts or practices or any of them should be declared to be unfair or deceptive within the meaning of this article.

The hearings provided by this section shall be conducted in accordance with the Administrative Procedure Act, Chapter 5 (commencing at Section 11500) of Part 1, Division 3, Title 2 of the Government Code, and the commissioner shall have all the powers granted therein. If the alleged methods, acts, or practices or any of them are found to be unfair or deceptive within the meaning of this article the commissioner shall issue and service upon said person his written report so declaring.

(b) If such report charges a violation of this article and if such method of competition, act or practice has not been discontinued, the commissioner may, through the Attorney General of this State, at any time after 30 days after the service of such report cause a petition to be filed in the superior court of this State within the county wherein the person resides or has his principal place of business, to enjoin and restrain such person from engaging in such method, act or practice. The court shall have jurisdiction of the proceeding and shall have the power to make and enter appropriate orders in connection wherewith and to issue such writs are ancillary to its jurisdiction or are necessary in its judgment to prevent injury to the public pendente lite.

(c) A transcript of the proceedings before the commissioner, including all evidence taken and the report and findings shall be filed with such petition. If either party shall apply to the court for leave to adduce additional evidence and shall show, to the satisfaction of the court, that such additional evidence is material and there were reasonable grounds for the failure to adduce such evidence in the proceeding before the commissioner, the court may order such additional evidence to be taken before the commissioner and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The commissioner may modify his findings of fact or make new findings by reason of the additional

evidence so taken, and he shall file such modified or new findings with the return of such evidence.

(d) If the court finds that the method of competition complained of is unfair or that the act or practice complained of is unfair or deceptive, that the proceeding by the commissioner with respect of the public and that the findings of the commissioner are supported by the weight of the evidence, it shall issue its order enjoining and restraining the continuance of such method of competition, act or practice.

§ 790.07. Violation of Cease and Desist Order; Hearing; Penalty; Review

Whenever the commissioner shall have reason to believe that any person has violated a cease and desist order issued pursuant to Section 790.05 or a court order issued pursuant to Section 790.06, after the order has become final, and while the order is still in effect, the commissioner may, after a hearing at which it is determined that the violation was committed, order that person to forfeit and pay to the State of California a sum not to exceed five thousand dollars ($5,000) plus any penalty due under Section 790.05, which may be recovered in a civil action, except that, if the violation is found to be willful, the amount of the penalty may be a sum not to exceed fifty-five thousand dollars ($55,000) plus the penalty due under Section 790.05.

For the purposes of this section, the failure to pay any penalty imposed pursuant to Section 790.035 which has become final shall constitute a violation of the cease and desist order.

For any subsequent violation of the cease and desist order or of the court order or the order to pay the penalty, while the order is still in effect, the commissioner may, after hearing, suspend or revoke the license or certificate of that person for a period not exceeding one year; provided, however, no such proceeding shall be based upon the subsequent

violation unless the same was committed or continued after the date on which the order imposing the penalty pursuant to the preceding paragraph became final.

The hearings provided by this section shall be conducted in accordance with the Administrative Procedure Act, and the commissioner shall have all the powers granted therein. The person shall be entitled to have the proceedings and the order of the commissioner therein reviewed by means of any remedy provided by Section 12940 or by the Administrative Procedure Act.

§ 790.08. Additional Powers of Commissioner

The powers vested in the commissioner in this article shall be additional to any other powers to enforce any penalties, fines or forfeitures, denials, suspensions or revocations of licenses or certificates authorized by law with respect to the methods, acts and practices hereby declared to be unfair or deceptive.

§ 790.09. Administrative Action Against License or Certificate; Civil Liability; Criminal Penalty

No order to cease and desist issued under this article directed to any person or subsequent administrative or judicial proceeding to enforce the same shall in any way relieve or absolve such person from any administrative action against the license or certificate of such person, civil liability or criminal penalty under the laws of this State arising out of the methods, acts or practices found unfair or deceptive.

§ 790.10. Rules and Regulations

The commissioner shall, from time to time as conditions warrant, after notice and public hearing, promulgate reasonable rules and regulations, and amendments and additions thereto, as are necessary to administer this article.

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No. 95-409

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1995

PROMETHEUS FUNDING CORP., etc., et al.,
Petitioners,
vs.
MERCHANTS HOME DELIVERY SERVICE, INC.,
Respondent.

On Petition for a Writ of *Certiorari* to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

Under the McCarran-Ferguson Act, 15 U.S.C. § 1012(b) ("MFA") which provides in relevant part that "[n]o Act of Congress shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance":

1. Do civil remedies in the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 *et seq.* ("RICO") "invalidate, impair or supersede" California's Unfair Insurance Practices Act, Cal. Ins. Code § 790 *et seq.* ("UIPA") because RICO's remedies are more severe than the civil remedies found in California law and is this question governed by state or reverse preemption of the field of insurance regulation or by traditional principles of implied federal preemption?

2. If RICO claims invalidate, impair or supersede the UIPA, are the following practices within the "business of insurance": fraud in taking money (a) for nonexistent insurance, (b) on fraudulently inflated premiums for actual insurance, and/or (c) for false claims?

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No. 95-409

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1995

PROMETHEUS FUNDING CORP., etc., et al.,
Petitioners,
VS.
MERCHANTS HOME DELIVERY SERVICE, INC.,
Respondent.

On Petition for a Writ of *Certiorari* to the United States Court of Appeals for the Ninth Circuit

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BRIEF FOR THE RESPONDENT IN OPPOSITION

DISCLOSURE AS TO RESPONDENT

Per rule 29.6, respondent discloses that National Freight Consortium, plc ultimately owns Merchants Home Delivery Service, Inc., a California corporation ("Merchants") through its other wholly-owned subsidiaries (namely, NFC International Holdings (Netherlands), Inc. which owns NFC International Holdings (USA), Inc. which owns Merchants). All subsidiaries of Merchants are wholly-owned by Merchants.

STATEMENT OF THE CASE

Merchants filed a civil action in the United States District Court, Central District of California, alleging civil RICO claims against its former broker, Frank B. Hall & Co., Inc. and associated defendants (collectively "Hall"), through which Merchants bought insurance.[1] (First Amended Complaint, Appellant's Excerpts of Record filed with the Court of Appeals for the Ninth Circuit, "ER" 1-74).

Merchants alleges that Hall stole at least $1.5 million in three ways (the "challenged practices"), taking Merchants' money *(1)* for the purchase of policies which were *never purchased* (ER 17-23, 31), *(2)* for premiums of actual policies which were *fraudulently marked up* in excess of the actual premiums set by underwriters (ER 17-18, 23-24) and *(3)* for *phony claims* (ER 17-18).[2]

Hall moved for judgment on the pleadings, arguing that the MFA expressly precluded federal civil claims as to the business of insurance. The district court granted that motion. (ER 179-189)

The Court of Appeals *unanimously* reversed and remanded. (Pet. App. 14a-25a) Thereafter, the Court of Appeals denied the petition for rehearing and rejected the suggestion for rehearing *en banc*. (Pet. App. 13a) The Court

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[1] For the text of RICO, see Pet. App. 26a.

[2] Merchants discovered other thefts and frauds in the state case (after judgment was entered in the federal case). This is a proper concern here in that judgment on the pleadings may be granted only if no set of facts entitle plaintiff to relief. *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957). Those additional frauds include (a) Hall's fraudulent conversion of trust funds to its own use including refunds not credited to Merchants and (b) other fraudulent compensation not disclosed to Merchants including commissions (since Merchants was to pay a "wholesale" price, i.e., no commissions) and interest on Merchants' money (in that Merchants was to get the cash flow benefits).

of Appeals applied a four part inquiry approved by this Court, focusing on the two contested questions. (Pet. App. 17a)

The first contested question below was whether the challenged practices constitute the "business of insurance." The Court of Appeals noted that the collection of premiums for phony policies does not spread any risk, does not create a relationship between insured and insurer and is not limited to entities in the insurance trade. Similarly, collection of money for phony claims is not the "business of insurance." Thus, Merchants could prosecute claims as to two of the three challenged practices (i.e., phony insurance and phony claims) irrespective of the answer to the second contested question. However, since one of the three practices was held to be the "business of insurance," the Court of Appeals needed to answer the second contested question.

The second contested question below was whether RICO "invalidates, impairs or supersedes" the UIPA.[3] The Court of Appeals agreed with the only other circuit court to address the standard for determining this prong of the MFA, *NAACP v. Amer. Family Mut. Ins. Co.*, 978 F.2d 287 (7th Cir. 1992), *cert. denied*, ____ U.S. ____, 113 S. Ct. 2335 (1993). The Court determined that the MFA did not completely abandon the field to the states and applied the "direct conflict" test traditionally used in cases of implied preemption, i.e., whether the federal law directly conflicted with the state law. (Pet. App. 23-25a) Since both federal and state law prohibit the challenged acts, the Court of Appeals concluded that there was no conflict and that RICO does not "invalidate, impair or supersede" California

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[3]For the text of the UIPA, see Pet. App. 27a-39a.

The question whether federal law "invalidates, impairs or supersedes" state law may dispose of the entire appeal. For that reason, this brief presents that question first (as does the Petition), i.e., reversing the order of questions in the Court of Appeals' decision.

law regulating insurance (Pet. App. 25a), so that Merchants may bring RICO claims based on each of the three challenged practices.

REASONS FOR DENYING THE PETITION

This Court has the tremendous benefit of receiving the position of the state regulators, who agree with the Court of Appeals' decision and vigorously oppose the petition, through their National Association of Insurance Commissioners ("NAIC"), the creator of the very Model Act on which California's UIPA is based.[4]

The petition should be denied for numerous reasons. The most fundamental reason is that no proper basis exists for this Court's discretionary review. There is no conflict between the circuit courts or between a circuit court and any state's highest court. Moreover, this Court either has previously addressed the question presented or the question involves facts highly specific to this case.

Second, the MFA did not create reverse "field preemption;" rather, as this Court noted in at least two decisions concerning the MFA, traditional federal preemption rules apply. The proper test under implied preemption is whether there is an "actual conflict" between RICO and state law. Based on no fewer than four (4) recent decisions of this Court, a difference in remedies does not create an "actual conflict."

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[4]NAIC filed an amicus brief below in support of Merchants' position and indicated that it also intends to file an amicus brief here.

Merchants urges this Court to first review the NAIC's brief and especially its description of the reliance by the various state insurance commissioners on RICO and on federal prosecutions to curb fraud in the business of insurance. It would be tragic if the wishes of the state regulators were disregarded in the name of the MFA's promotion of state regulation of insurance.

Third, the issue whether the challenged practices constitute the "business of insurance" (a) is moot since RICO and the UIPA coexist without actual conflict, and (b) is entirely case specific so as not to merit this Court's attention.

Fourth, the field preemption proposed by Hall is dangerous in that it would (a) bar criminal RICO prosecution as well as civil RICO prosecution, (b) bar all federal action whether based on interstate commerce, control of the mails or other federal function, and (c) create unnecessary legal complications as to choice of law, jurisdiction and venue where the fraud is truly interstate.[5] The MFA simply does not provide such gratuitous immunity for fraud in the insurance industry.

I.

THERE IS NO PROPER BASIS FOR REVIEW.

This Court's own rules shows that this case is inappropriate for review. Sup. Ct. R. 10. The principal basis for review — a conflict between the circuit courts — does not exist here. By only citing conflicting decisions in *district* and *intermediate state* courts (Pet. 13), the petition highlights its own inappropriateness.[6]

Instead, apparently under Rule 10(c), the Petition purports to present issues of "nationwide importance implicating paramount federal statutory policies." (Pet. 8) Setting

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[5]There is a question whether California regulation could reach all of the fraud since more than $1 million of Merchants' funds went to Hall's Texas subsidiary.

[6]The divergence of opinion is based on the failure by those courts to apply this Court's preemption analysis. The lower courts now have guidance from the Court of Appeals' decision and can correctly decide future cases.

aside the fact that every petitioner probably considers their position to be one of nationwide importance, Hall has not cited standards by which the nationwide importance of its petition can be measured.[7] The argument also ignores Rule 10(c) which limits review to questions which have not been but should be decided by this Court. The questions here either have been decided by, or are inappropriate for, this Court.

This Court previously declined *certiorari* on the very issue presented here, namely whether civil RICO was barred by the MFA. *American Int'l. Group, Inc. v. Superior Court*, 285 Cal. Rptr. 765 (Ct. App. 1991), *cert. denied, Brutoco Eng. & Const. v. American Int'l. Group, Inc.*, 504 U.S. 911 (1992).[8] There are no new circumstances to justify a change in the Court's position. In addition, by declining *certiorari* in *NAACP*, this Court correctly declined to revisit the standard for implied preemption cases, namely whether there is a direct conflict between the federal and state laws.

The question whether federal law "invalidates, impairs or supersedes" state law, has no greater urgency now than when this Court denied *certiorari* in *NAACP* and *Brutoco*. If there was ever any confusion on this topic, this Court cleared it up in its most recent decision on the MFA, *U.S. Dept. of Treas. v. Fabe* ____U.S.____, 113 S. Ct. 2202, 2211 (1993), by holding that federal and state laws coexist except to the extent of a direct conflict. Moreover, the question whether differences in federal and state remedies constitute

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[7] Hall's argument as to increase in litigation and product cost undoubtedly are common arguments to this Court and hardly show "nationwide importance."

[8] *AIG* was not only wrongly decided but presented an even better case for *certiorari* for its complete disregard of preemption law. Here, the Court of Appeals applied preemption law. Any complaint that the Court of Appeals incorrectly applied that law is a disfavored basis for *certiorari*. Sup. Ct. R. 10.

an actual conflict has been answered by this Court in at least four (4) recent decisions.

The question whether the challenged practices constitute the "business of insurance," involves facts specific to this case rather than a matter of national importance. In *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982), this Court provided the analysis to help lower courts with this topic and there is no need for this Court to review each application of *Pireno*'s analysis.

As this Court has previously pointed out, any displacement of civil RICO will also displace criminal RICO. *English v. General Elec. Co.*, 496 U.S. 72, 83 (1990) ("Acceptance of respondent's argument would require us to conclude that Congress has displaced not only state tort law, which is at issue in this case but also state *criminal* law.") Thus the limits on civil RICO demanded by Hall would also tie the hands of federal criminal authorities in prosecuting fraud in the "business of insurance."

The floodgates argument (i.e., that substantially more RICO cases will now be filed than if Hall's position were accepted) (Pet. 20) is factually wrong and constitutionally inappropriate. Since this Court's careful clarification of the "pattern" requirement in RICO set forth in *H.J., Inc. v. Northwestern Bell Tel. Co.*, 492 U.S. 229 (1989), the number of RICO filings has declined. *See* Admin. Office of the U.S. Courts, 1992 Annual Report at Table C-A2 (there were *1129* RICO filings out of 225,811 filings in 1989 and *897* out of 230,503 in 1992); Resp. App. 1a. Moreover, as this Court also noted in *H.J.*, if RICO is to be further restricted, "it is a job for Congress." *H.J.*, 492 U.S. at 249.

This Court need go no further in this brief for reasons to deny the Petition. It need not burden itself with review of each application of its decisions. There are no new or emergency circumstances to justify a change of existing

preemption principles. There is no split of authority which would justify review under this Court's own rules. Simply, review would be a unjustifiable waste of this Court's time.

II.

RICO'S CIVIL REMEDIES DO NOT INVALIDATE, IMPAIR OR SUPERSEDE THE UIPA.

A. Federal Law Yields To State Insurance Regulation Only To The Extent Of An Actual Conflict.

Hall asserts that the Court of Appeals applied an incorrect standard (namely the actual conflict standard used in implied preemption cases), that "this Court has never said that such an actual or direct conflict is needed to come within McCarran-Ferguson" (Pet. 8) and that the MFA created "state law preemption of federal law" (Pet. 8-9).[9] In essence, Hall interprets the MFA as creating a new type of preemption, never before recognized by this Court, in the form of a reverse field preemption — that state law regulating any part of the business of insurance ousts all federal law from that entire field. (*Compare* Pet. 9, "states have primary jurisdiction" and "state law preemption of federal

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[9]This argument represents an extreme retreat in Hall's position. According to the District Court and Hall, there was an actual conflict between RICO and California law. RICO's remedies (treble damages and attorneys' fees) would, according to the District Court, "supersede the state remedies," (Pet. App. 10a) and would according to Hall, "upset the balance struck by California's insurance code" (Pet. 23a).

After Merchants cited below no less than four decisions of this Court that different remedies do not create a conflict under preemption law, Hall retreated from its previous position (that the difference in remedies created a conflict) to now argue that "actual conflict" is not required and that the MFA created a novel type of reverse field preemption.

law"). The Court of Appeals agreed that Hall was advocating a reverse field preemption:

> This argument amounts to the contention that Congress intended the McCarran-Ferguson Act to allow states to *preempt the field* in the regulation of the business of insurance.

Pet. 23a (emph. added).

As shown below, under this Court's decisions, the field preemption argument is clearly incorrect. Pursuant to traditional principles of implied preemption, federal law is only ousted where it actually or directly conflicts with state law. The correct statement of the operation of the MFA is that it allows the states to regulate insurance, allows Congress to apply any law to the business of insurance except that to the extent that the federal and state laws conflict, federal law must yield.[10]

Hall cited *FTC v. National Cas. Co.*, 357 U.S. 560, 563-64 (1958) in support of its position that federal law may not even supplement state law regulating the business of insurance (Pet. 10-11) and that an actual conflict between federal and state law is not required to invoke the MFA (Pet. 19). *FTC* is not at all appropriate here since *FTC* is based on a *different* portion of the MFA as seen below:

> No Act of Congress shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insur-

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[10] In addition, under the MFA, a federal law may "specifically relate[ ] to the business of insurance", in which case Congress apparently can still preempt the state regulation. While RICO does not specifically relate to the business of insurance (and thus does not preempt state law in the event of a conflict), this part of the MFA helps to show that the MFA did not create reverse field preemption, as further explained below.

> ance: *Provided*, That after June 30, 1948, * * * the Sherman Act, * * * the Clayton Act, and * * * the *Federal Trade Commission Act* * * * shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

15 U.S.C. § 1012(b) (emph. added).

The Federal Trade Commission is subject to the second sentence (the proviso); it may regulate only "to the extent that such business is not regulated by State law." *Id.* In contrast, this case is subject to the first sentence so that RICO may not "be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance." *Id.* The two sentences significantly differ in obvious ways.[11] The first sentence requires a determination of whether the federal law "invalidates, impairs or supersedes" the state law.[12] The proviso does not require such a determination. It is thus highly

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[11] Hall itself recognized a "significant difference" between the two sentences of the MFA. (Pet. 23)

[12] The phrase "invalidates, impairs or supersedes" is meaningless unless it requires some scrutiny of the interplay between the federal and state laws.

If the MFA created field preemption, the first sentence would read like the proviso — without the phrase "invalidates, impairs or supersedes".

If the MFA allowed no differences between federal and state laws, then it would have created an express preemption — that the federal government could not regulate the business of insurance at all. Yet the MFA does not so read.

The standard under the MFA is necessarily one of implied preemption which allows the statutes to coexist absent a conflict. The words themselves — invalidate, impair and supersede — focus on whether there is a conflict and do not provide for either field preemption or express preemption.

inappropriate for Hall to argue that *FTC* applies here.[13] Significantly, this Court did not even mention *FTC* in *Fabe*, its most recent decision on the MFA.

Hall also cited *SEC v. National Securities, Inc.*, 393 U.S. 453 (1969) to support its argument that the MFA created field preemption. (Pet. 10) In *SEC*, the Arizona Insurance Commissioner *approved* a merger involving an insurance company which the SEC then sought to *unwind* (along with other remedies) for violations of federal securities laws (including Rule 10b-5). Recognizing that regulation of an activity may come from multiple government agencies, this Court rejected the insurance company's position as follows:

> [Respondents] contend that any attempt to interfere with a merger approved by state insurance officials would "invalidate, impair or supersede" the state insurance laws made paramount by the McCarran-Ferguson Act. We cannot accept this overly broad restriction on federal power.
>
> It is clear that any "impairment" in this case is a most indirect one.... Arizona has not commanded something which the Federal Government seeks to prohibit. It has permitted respondents to consummate the merger; it did not order them to do so.... The paramount federal interest in protecting shareholders is in this situation perfectly compatible with the para-

[13] Moreover, *FTC* is a terse, three-page, forty-year-old decision which predates, and thus could not apply, the four-prong test (first developed in *Cochran v. Paco, Inc.*, 606 F.2d 460, 464 (5th Cir. 1979)) which all parties agree was properly used in this case. The very terseness of the decision reflects the simple nature of the single issue before the court — whether the state regulated insurance. Moreover, *FTC* concerned apples and apples (actual regulation by both federal and state governments) whereas this case involves apples and oranges (state insurance regulation and citizens' civil remedies against racketeering).

> mount state interest in protecting policyholders . . . In these circumstances, we simply cannot see the *conflict.*

SEC, 393 U.S. at 463 (emph. added).

It is not mere coincidence that *SEC* addresses the absence of a "conflict." Most recently, this Court invoked the conflict standard in *U.S. Dept of Treas v. Fabe*, ____ U.S. ____, 113 S. Ct. 2202 (1993), a case in which the parties stipulated that the federal and state laws were in direct conflict (since the federal law placed the United States government in first position as a creditor of an insolvent insurer whereas Ohio law gave policyholders, other expenses and other creditors a higher priority than the United States).

In *Fabe*, this Court did not hold that the direct conflict allowed state law to govern the entire field. This Court did not hold that due to the direct conflict federal law was completely ousted or barred. Rather, this Court explained the effect of the MFA in the following way:

> Ordinarily, a federal law supersedes any inconsistent state law. The first clause of § 2(b) [of the McCarran-Ferguson Act] reverses this by imposing what is, in effect, a clear-statement rule, a rule that state laws enacted "for the purpose of regulating the business of insurance" do not yield to *conflicting* federal statutes unless a federal statute specifically requires otherwise.

Fabe, 113 S. Ct. at 2211 (emph. added).

This passage makes at least two important points. First, the MFA allows state law to avoid or be exempt from federal preemption.[14] *Id.* at 2212 (noting that *Group Life &*

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[14]This *exemption from federal preemption* is not the same thing as *reverse field preemption.* Field preemption would allow the states to occupy the entire field by regulating any part of the business of insurance, resulting in complete ouster of federal law from the entire

Health Ins. Co. v. Royal Drug Co., 440 U.S. 205, 217 (1979), "rejected the notion that such indirect effects are sufficient for a state law to avoid [federal] pre-emption under the McCarran-Ferguson Act"). In other words, the state's avoidance of federal preemption means that the federal and state laws coexist unless they cannot coexist, i.e., a conflict allows the state law to displace the federal law. The Court of Appeals' analysis obeys traditional preemption principles and maximizes the coexistence of federal and state regulations. Hall's analysis invents a new species, a reverse field preemption which has no explicit basis in the case law.

Second, *Fabe* holds that a federal law must yield only if it conflicts with, and *only to the extent* that it conflicts with, a state law whose purpose is the regulation of the business of insurance:

> In the present case . . . there is a *direct conflict* between the federal priority statute and Ohio law . . . therefore, federal law must yield *to the extent* the Ohio statute furthers the interests of policyholders.

Fabe Id. at 2208 (emph. added).

There is substantial case law on the question of "actual conflict." Actual conflict exists "when it is impossible to comply with both state and federal law." *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248 (1984); *See English*, 496 U.S. at 79. Actual conflict is synonymous with "irreconcilable conflict." *Silkwood*, 464 U.S. at 256. In areas of coincident federal and state regulation, the "teaching of this Court's decisions . . . enjoin[s] seeking out conflicts between state and federal regulation where none clearly ex-

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field. Exemption from federal preemption means that state and federal laws each apply to the business of insurance except in the event of a direct conflict.

ists." *Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440, 446 (1960).

Hall appears to argue that any state could ignore long standing preemption principles and define for itself the nature of its preemption in the business of insurance. For example, under this argument, California could explicitly legislate that the only remedies are those in the UIPA (its law regulating the business of insurance) and that federal civil remedies are not available to remedy wrongs in the business of insurance. Even if, for argument's sake, California could expressly preempt all remedies other than those in the UIPA, California has not done so.[15]

Hall suggests that *SEC* was decided, not on the issue of "conflict," but on the distinction that the entities operated in different "*spheres*," i.e., the state protected policyholders and the SEC protected shareholders. (Pet. 10) This distinction breaks down in light of this Court's opinion as quoted above (concerning the absence of a conflict) and its conclusion that:

> [I]t has never been held that state regulation of insurance securities pre-empts federal regulation, on the theory that the federal securities laws would be "superseding" state laws regulating the business of insurance. The fact that Arizona purports to protect the interests of insurance company stockholders does not,

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[15] As explained below, California does not restrict remedies to those remedies in the UIPA. On the one hand, there are no civil remedies in the UIPA and on the other hand, California makes available various remedies for fraud in the business of insurance. *Moradi-Shalal v. Fireman's Fund Ins. Cos.*, 250 Cal. Rptr. 116, 127, 758 P.2d 58, 68-69 (1988). In addition, civil RICO claims may be filed in California courts. *Cianci v. Superior Court*, 221 Cal. Rptr. 575, 576, 710 P.2d 375, 381 (1985).

> therefore, by itself, render the federal securities laws inapplicable.

SEC, 393 U.S. at 461.

Nonetheless, even under Hall's interpretation, i.e., that *SEC* allowed coexisting regulations only if each was in its own sphere (the SEC's sphere being protection of shareholders and the Insurance Commissioners's sphere being protection of policyholders), the same approach is true here with the federal sphere being protection from criminal racketeering and the state sphere being ratemaking and licensing.[16]

Where there is incomplete displacement of the other body of law, the preemption standard is necessarily the "conflict" standard. *Cal. Fed. S. & L. Ass'n. v. Guerra*, 479 U.S. 272, 281 (1987) and *Cal. Coastal Comm'n. v. Granite Rock Co.*, 480 U.S. 572, 581 (1987). The MFA contains two provisions which render its displacement of federal law unquestionably incomplete so that it could not possibly create field preemption — that phrase mentioned above (namely that federal law is displaced only if it "invalidates, impairs or supersedes" state law) and the language that Congress can preempt the states' power to regulate insurance by any law which "specifically relates" to insurance. Since the displacement of federal law is incomplete, the conflict standard necessarily applies.

Logic and language compel the same result. The very language of the MFA does not provide for field or express preemption since the MFA preempts federal law only if the federal law "invalidates, impairs or supersedes" the state

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[16] In discussing *SEC*, Hall acknowledged that federal interference is not barred where it is too "indirect" in light of the importance of the federal action (Pet. 10). Once again, the test is conflict since "interference" necessarily refers to the interplay of federal and state laws, namely whether the federal law conflicts with the state law.

law. The phrase "invalidates, impairs or supersedes" is necessarily descriptive of "conflict."[17] If the MFA were to provide for express preemption, this determination, (of whether the federal law "invalidates, impairs or supersedes" the state law) would not have been included in the MFA.

Since this Court has applied the conflict test in *SEC* and *Fabe*, there should be no doubt that the MFA only applies if federal law conflicts with state law. As noted below, other decisions of this Court show that the difference of remedies do not create an actual conflict between RICO and California law.

B. A Difference In Remedies Is Not A Conflict.

No less than four decisions of this Court show that the Court of Appeals correctly decided that RICO does not conflict with any California law enacted for the purpose of regulating the business of insurance. The law is so clear that review of this case is just not needed.

First, no conflict is created by a difference in remedies between the federal and state laws. In *Silkwood*, this Court rejected the United States' argument that the state punitive damage award (based on radiation safety violations) conflicts with the NRC's authority to impose civil penalties. *Silkwood*, 464 U.S. at 257. Even though the punitive damage award was clearly intended to punish operators for safety

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[17]The words "invalidate," "impair" and "supersede" express the same concept as "conflict," "interfere," "contravene" used in preemption cases. *See, e.g., Southern Pac. Co. v. Jensen*, 244 U.S. 205, 216 (1917) ("interfere" and "contravene"); *Chevron U.S.A., Inc. v. Hammond*, 726 F.2d 483, 488 (9th Cir. 1984), *cert. denied*, 471 U.S. 1140 (1985) ("superseded").

violations, which is a function reserved to the NRC, this Court found no conflict and pointed out that:

> Paying both federal fines and state-imposed punitive damages for the same incident would not appear to be physically impossible. Nor does exposure to punitive damages frustrate any purpose of the federal remedial scheme.

Id.

This Court noted that "tension" may exist since safety regulation is an exclusively federal concern and state punitive damage awards for safety violations may have a policing effect. *Id.* at 256. However, this Court warned that such tension between federal and state law must be tolerated. *Id.* This Court rejected "field preemption" even for a subject as critical as nuclear safety:

> [I]nsofar as damages for radiation injuries is concerned, preemption should not be judged on the basis that the Federal Government has so completely occupied the field of safety that state remedies are foreclosed but on whether there is an *irreconcilable conflict* between the federal and state standards or whether the imposition of a state standard in a damages action would frustrate the objectives of the federal law.

Id.

Here, RICO provides for treble damages and attorneys' fees. While California law does not provide treble damages for fraud, it provides for punitive damages (Cal. Civ. Code § 3294; Resp. App. 1a); double damages (Cal. Probate Code § 16249(b); Resp. App. 3a); attorneys' fees in appropriate cases (Cal. Code of Civ. Proc. § 1021; Resp. App. 2a) and fines up to $55,000 (*Moradi-Shalal v. Fireman's Fund Ins. Cos.*, 250 Cal. Rptr. 116, 127, 758 P.2d 58, 68-69 (1988)). As noted above, those differences do not create a

conflict since a damages award does not violate or overturn state law. *Silkwood*, 464 U.S. at 257.

Second, the absence of certain remedies does not imply any intent to reject those remedies. *English*, 496 U.S. at 89; *Silkwood*, 464 U.S. at 251 (absence of federal civil remedies was considered evidence of an intent not to preempt state civil remedies). This Court wrote:

> The District Court also relied on the absence in § 210 [the federal law] of general authorization for the Secretary to award exemplary damages against employers who engage in retaliatory conduct. The District Court concluded, and respondent now argues, that this absence implies a congressional intent to bar a state action, like petitioner's, that permits such an award . . . We believe the District Court and respondent have read too much into Congress' decision not to authorize exemplary damages for most § 210 violations.

English, 496 U.S. at 89.

Even the California Supreme Court agreed that "something more than mere silence should be required before that [legislative] acquiescence is elevated into a species of implied legislation." *Cianci v. Superior Court*, 221 Cal. Rtpr. 575, 586, 710 P.2d 375, 386 (1985). Thus, the silence of the UIPA on the issue of damages must not generate a conclusion that California decided not to allow treble damages and attorneys' fees for broker fraud, especially where California's remedies are set forth in laws other than the UIPA and where California law provides for attorneys' fees, treble damages, double damages and punitive damages.

Third, one forum may "supplement" another forum's law without creating a conflict. In *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 112 S. Ct. 2608 (1992), this Court held that state common law claims against cigarette manufactur-

ers were not preempted by federal laws regulating warning labels, stating:

> In the absence of an express congressional command, state law is pre-empted if that law actually conflicts with federal law, [Supreme Court citation omitted], or if federal law so thoroughly occupies a legislative field "as to make reasonable the inference that Congress left no room for the States to supplement it." *Fidelity Fed. Sav. & Loan Assn. v. De la Cuesta*, 458 U.S. 141, 153 (1982) (quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. at 230).

Cipollone, 505 U.S. at ____, 112 S. Ct. at 2617.

Fourth, no conflict arises merely from additional liabilities or harsher remedies in one forum. In *Cal. v. ARC America Corp.*, 490 U.S. 93, 105 (1989), this Court held that "ordinarily, state causes of action are not pre-empted solely because they impose liability over and above that authorized by federal law."

California provides a number of remedies which are not based on the UIPA, the law which the MFA would treat as the "law enacted for the purpose of regulating the business of insurance." Punitive damages may be available for fraud, conversion or other tortious conduct. Cal. Civ. Code § 3294. Double damages may be available for diversion of trust funds. Cal. Probate Code § 16249(b). Rescission and other remedies may be available under equitable claims. Differing legal remedies have always co-existed and Hall cites no authority that a conflict arises from the differences.[18]

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[18]This Court has pointed out that cumulative remedies advance remedial statutes. *Herman & MacLean v. Huddleston*, 459 U.S. 375, 386 (1983).

C. It Is Immaterial Whether RICO's Remedies Invalidate, Impair Or Supersede Laws *Not* "Enacted For The Purpose Of Regulating The Business Of Insurance."

Here, RICO's remedies could not interfere with the remedies in the UIPA since that law does not contain any civil remedies.

The MFA only applies if RICO invalidates, impairs or supersedes a California law "enacted for the purpose of regulating the business of insurance." If RICO supersedes a law other than one enacted to regulate insurance, the MFA does not apply. It is clear that the UIPA is California's law "enacted for the purpose of regulating the business of insurance." Hall agrees. (Pet. 15-16)

It is also clear that, according to the California Supreme Court, the source in California of civil remedies arising from fraud in the business of insurance is not the UIPA. *Moradi-Shalal*, 250 Cal. Rtpr. at 127, 758 P.2d at 68-69. Rather, civil remedies are based on law other than the UIPA:

> The courts retain jurisdiction to impose civil damages or other remedies against insurers in appropriate common law actions, based on such traditional theories as fraud, infliction of emotional distress and (as to the insured) either breach of contract or breach of the implied covenant of good faith and fair dealing. Punitive damages may be available in actions not arising from contract where fraud, oppression or malice is proved.

Id.

Since the UIPA is silent as to civil remedies and since California permits civil damages and other remedies, RICO's remedies necessarily do not supersede the UIPA, the "law enacted for the purpose of regulating the business of insurance."

D. Other Reasons Support The Court Of Appeals' Decision.

While the MFA is concerned with duplicative federal licensing or taxation based on an expansion of the Commerce Clause, it is a very different thing to bar RICO's protection of citizens from criminal racketeering. RICO's origin is not solely the Commerce Clause and, consistent with this view, criminal prosecution for mail fraud in the business of insurance has not been barred by the MFA. *U.S. v. Sylvanus*, 192 F.2d 96 (7th Cir. 1951), *cert. denied*, 342 U.S. 943 (1952).[19]

It is one thing to compare federal and state regulations. It is a very different and awkward thing to compare a citizen's federal remedies with state regulation. Indeed, this Court has consistently rejected limits on citizen remedies based on such comparisons. *See, e.g., Silkwood; English; Cipollone* and *ARC America.*

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[19] *See also Russello v. U.S.*, 464 U.S. 16 (1983) (affirming a RICO conviction for fraudulent receipt of insurance proceeds); *U.S. v. Starnes*, 644 F.2d 673 (7th Cir. 1981), *cert. denied*, 454 U.S. 826 (1981) (affirming a RICO conviction for insurance fraud).

RICO was intended to augment other criminal laws and not limit or be limited by them. *U.S. v. Angelilli*, 660 F.2d 23, 34 (2d Cir. 1981), *cert. denied*, 455 U.S. 945 (1982). RICO has a stronger link to Penal Code § 487 (under which the felons were convicted; Resp. App. 3a, 4a) than to the UIPA. § 487 concerns grand theft and is not a law whose purpose is the regulation of the business of insurance. As this Court noted in *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 50 (1987):

> A common-sense view of the word "regulates" would lead to the conclusion that in order to regulate insurance, a law must not just have an impact on the insurance industry, but be specifically directed toward that industry.

III.

THE "BUSINESS OF INSURANCE" DOES NOT INCLUDE FRAUD IN TAKING MONEY (A) FOR NONEXISTENT INSURANCE, (B) ON FRAUDULENTLY INFLATED PREMIUMS, AND/OR (C) FOR FALSE CLAIMS.

Hall aserts that the taking of money for fictitious insurance and phony claims are practices which constitute the business of insurance.

First, unless this Court determines that RICO "invalidates, impairs or supersedes" the UIPA, this question is entirely moot because, irrespective of the answer to this question, Merchants can prosecute its RICO claims since they do not conflict with California insurance regulation.

Second, the issue as to whether the challenged practices are the "business of insurance" is so case-specific as to not require review by this Court.

Third, the Court of Appeals here properly invoked and applied the correct factors, set out in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129 (1982), to determine whether the challenged practices are the "business of insurance." The Court of Appeals correctly decided that Hall's receipt of monies for phony, nonexistent policies and for phony, nonexistent claims is not the "business of insurance" but the business of crime.[20]

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[20]The state response was by the District Attorney (felony conviction based on Penal Code for grand theft including restitution to victims) rather than by the Insurance Commissioner (no action taken pursuant to the UIPA to help victims).

Indeed, this Court's language in *H.J.* suggests that this type of activity could be the basis for a RICO claim:

> A RICO pattern may surely be established . . . Suppose a hoodlum were to sell "insurance" to a neighborhood's storekeepers to cover them against breakage of their windows, telling his victims he would

The Court of Appeals' conclusion tracks statements of this Court, in *SEC v. Variable Annuity Life Ins. Co. of America*, 359 U.S. 65, 71 (1959) ("The concept of 'insurance' involves some investment risk-taking on the part of the company") and *Group Life & Health Ins. Co. v. Royal Drug*, 440 U.S. 205, 212 (1979) (underwriting or spreading of risk is "an indispensable characteristic of insurance") and 440 U.S. at 226-7 ("The legislative history makes clear that Congress did not intend the definition of the 'business of insurance' to be broader than its commonly understood meaning").

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be reappearing each month to collect the "premium" that would continue their coverage.

H.J., 492 U.S. at 242.

CONCLUSION

The petition for a writ of *certiorari* should be denied.

DATED: October 2, 1995

Respectfully submitted,

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APPENDIX A

1992 ANNUAL REPORT OF THE DIRECTOR
L. RALPH MECHAM
ACTIVITIES OF THE ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS

Table C-2A
U.S. District Courts — Civil Cases Commenced by Nature of Suit During the 12 Month Periods Ending September 30, 1988 through 1992

Nature of Suit	1988	1989	1990	1991	1992	Percent Change 1991/1991
* * *						
RICO	941	1,129	1,138	972	897	-7.7
* * *						

California Civil Code § 3294; Availability of exemplary damages

(a) In an action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud or malice, the plaintiff, in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant.

(b) An employer shall not be liable for damages pursuant to subdivision (a), based upon acts of an employee of the employer, unless the employer had advance knowledge of the unfitness of the employee and employed him or her with a conscious disregard of the rights or safety of others or authorized or ratified the wrongful conduct for which the damages are awarded or was personally guilty of the oppression, fraud or malice. With respect to a corporate employer, the advance knowledge and conscious disregard, authorization, ratification or act of oppression, fraud or malice must

be on the part of an officer, director, or managing agent of the corporation.

(c) As used in this section, the following definitions shall apply:

(1) "Malice" means conduct which is intended by the defendant to cause injury to the plaintiff or despicable conduct which is carried on by the defendant with a willful and conscious disregard of the rights or safety of others.

(2) "Oppression" means despicable conduct that subjects a person to cruel and unjust hardship in conscious disregard of that person's rights.

(3) "Fraud" means an intentional misrepresentation, deceit, or concealment of a material fact known to the defendant with the intention on the part of the defendant of thereby depriving a person of property or legal rights or otherwise causing injury.

(d) Damages may be recovered pursuant to this section in an action pursuant to Chapter 4 (commencing with Section 377.10) of Title 3 of Part 2 of the Code of Civil Procedure based upon a death which resulted from a homicide for which the defendant has been convicted of a felony, whether or not decedent died instantly or survived the fatal injury for some period of time. The procedures for joinder and consolidation contained in Section 377.62 of the Code of Civil Procedure shall apply to prevent multiple recoveries of punitive or exemplary damages based upon the same wrongful act.

(e) The amendments to this section made by Chapter 1498 of the Statutes of 1987 apply to all actions in which the initial trial has not commenced prior to January 1, 1988.

California Code of Civil Procedure § 1021; Attorney fees and costs, generally

Except as attorney's fees are specifically provided for by statute, the measure and mode of compensation of attorneys and counselors at law is left to the agreement, express or implied, of the parties; but parties to actions or proceedings are entitled to their costs, as hereinafter provided.

California Probate Code § 16249(b); Actions and proceedings; wrongful taking, concealing or disposing of trust property/liability.

(b) A person who, in bad faith, has wrongfully taken, concealed, or disposed of property in or belonging to the trust is liable for twice the value of the property, recoverable in an action by a trustee for the benefit of the trust.

California Penal Code § 487; Grand Theft.

Grand theft is theft committed in any of the following cases:

1. When the money, labor or real or personal property taken is of a value exceeding four hundred dollars ($400); provided, that when domestic fowls, avocados, olives, citrus or deciduous fruits, other fruits, vegetables, nuts, artichokes, or other farm crops are taken of a value exceeding one hundred dollars ($100); provided, further, that when fish, shellfish, mollusks, crustaceans, kelp, algae, or other aquacultural products are taken from a commercial or research operation which is producing that product, of a value exceeding one hundred dollars ($100); provided, further, that where the money, labor, real or personal property is taken by a servant, agent or employee from his principal or employer and aggregates four hundred dollars ($400) or more in any 12 consecutive month period, then the same shall constitute grand theft.

For purposes of establishing that the value of avocados or citrus fruit under this subdivision exceeds one hundred dollars ($100), that value may be shown by the presentation of credible evidence which establishes that on the day of the theft avocados or citrus fruit of the same variety and weight exceeded one hundred dollars ($100) in wholesale value.

2. When the property is taken from the person of another.

3. When the property taken is an automobile, firearm, horse, mare, gelding, any bovine animal, any caprine animal, mule, jack, jenny, sheep, lamb, hog, sow, boar, gilt, barrow or pig.

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No. 95-409

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

PROMETHEUS FUNDING CORP., ETC., *et al.*,
Petitioners,
v.
MERCHANT HOME DELIVERY SERVICES, INC.,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF AMICI CURIAE, NATIONAL ASSOCIATION OF INDEPENDENT INSURERS, AMERICAN INSURANCE ASSOCIATION, ALLIANCE OF AMERICAN INSURERS, AND AMERICAN COUNCIL OF LIFE INSURANCE IN SUPPORT OF PETITIONERS

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BRIEF OF AMICI CURIAE, NATIONAL ASSOCIATION OF INDEPENDENT INSURERS, AMERICAN INSURANCE ASSOCIATION, ALLIANCE OF AMERICAN INSURERS, AND AMERICAN COUNCIL OF LIFE INSURANCE IN SUPPORT OF PETITIONERS

This brief is submitted by the National Association of Independent Insurers, the American Insurance Association, the Alliance of American Insurers and the American Council of Life Insurance (hereinafter "Amici") in support of the Petition for Writ of Certiorari filed by Prometheus Funding Corporation, et al ("Petitioners") seeking review of the decision of the Court of Appeal for the

Ninth Circuit in *Merchant Home Delivery Service, Inc. v. Frank B. Hall & Co. et al*, 50 F.3d 1486 (9th Cir. 1995) ("*Merchant Home Delivery*"). Amici urge the Court to grant the petition.[1]

STATEMENT OF INTEREST OF AMICI

The National Association of Independent Insurers ("NAII") is a volunteer, nonprofit insurance trade association. Its 570 member companies primarily write property and casualty insurance in the United States. The American Insurance Association ("AIA") is a volunteer, non-profit insurance trade association with approximately 270 member property-casualty insurers country-wide. The Alliance of American Insurers ("AAI") is a volunteer, non-profit insurance trade association representing more than 220 property-casualty insurance companies nationwide. The American Council of Life Insurance ("ACLI") is a volunteer, non-profit insurance trade association with more than 600 member life and health insurance companies country-wide. All four Amici regularly appear, on behalf of their members, before Congress and state legislatures, regulatory agencies and courts.

Amici collectively represent a broad spectrum of the insurance industry in the United States. Their members include both large insurers serving national markets and small specialty and regional insurers. The Amici also represents both the property-casualty and the life-health branches of the insurance industry. Amici, therefore, bring a different perspective to this case than the other parties. Amici are concerned about the implications of the Ninth Circuit's ruling for their members' operations throughout this country and the probability that the Ninth Circuit's decision will generate a significant increase in

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[1] All parties have consented to the filing of amicus curiae briefs in connection with the Petition for Writ of Certiorari in this matter and letters documenting that consent have been filed with the Court.

claim defense and settlement costs as routine claim and coverage disputes become Racketeer Influenced and Corrupt Organizations Act ("RICO") cases.

SUMMARY OF ARGUMENT

Amici submit that this case was wrongly decided as a matter of law. The Ninth Circuit's decision in *Merchant Home Delivery* will disrupt insurer operations in California and other states by substantially narrowing the scope of the McCarran-Ferguson Act, which gives the states plenary authority over the business of insurance. The decision is also a major step toward the "federalization" of insurance regulation, since the Ninth Circuit reached a diametrically opposite conclusion from the California appellate court which had previously held that allowing RICO remedies would impair California's insurance regulatory scheme. Given the conflict among the federal courts and between federal and state courts concerning the availability of RICO remedies in litigation involving insurance claims, *Merchant Home Delivery* will exacerbate the problem of inconsistent results across jurisdictions already faced by insurers. If not reversed, the *Merchant Home Delivery* decision is likely to significantly increase insurers' defense costs in what previously were routine cases and, therefore, the cost of insurance to their policyholders.

ARGUMENT

I. WHETHER RICO REMEDIES ARE AVAILABLE IN ROUTINE INSURANCE DISPUTES IS OF MAJOR IMPORTANCE TO INSURERS AND THEIR POLICYHOLDERS WHO WILL FACE HIGHER COSTS IN THE WAKE OF *MERCHANT HOME DELIVERY*.

A. The *Merchant Home Delivery* Decision Fundamentally Undercuts Congress' Determination That Insurance Should Be Regulated By The States.

In holding that the application of RICO to the Petitioners' actions would not "invanidate, impair, or supersede" California law, the Court below has significantly intruded into state regulation of insurance. *Merchant Home Delivery v. Hall & Co., supra*, 50 F.3d at 1492. This intrusion is contrary both to the letter and the spirit of the McCarran-Ferguson Act, 15 U.S.C.A. 1011 *et seq.* The McCarran-Ferguson Act was enacted by Congress to preserve the traditional authority of the states to regulate insurance following this Court's 1944 decision in *United States v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944). *South-Eastern Underwriters* held that insurance was in interstate commerce and, therefore, subject to federal law under the Commerce Clause. In order to maintain state regulatory authority over insurance, Congress passed the McCarran-Ferguson Act, which provides in pertinent part: "No Act of Congress shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance." *See Group Life and Health Insurance Co. v. Royal Drug Co.*, 440 U.S. 205, 218-219 (1979) (purpose of McCarran-Ferguson is to preserve state regulation of insurance as it existed before *South-Eastern Underwriters*).

In this case, the Ninth Circuit ruled that application of RICO to overcharges for insurance coverage did not "in-

validate, supersede or impair" California's insurance regulatory laws. California has enacted a comprehensive scheme regulating premiums charged for property-casualty insurance, the type of coverage at issue in this case. Rates are required to be filed with and approved by the Department of Insurance. Cal. Ins. Code § 1861.01. The charging of a rate other than the rate approved by the Commissioner of Insurance is prohibited under Section 1858.07 of the California Insurance Code which provides:

> Any person who uses any rate, rating plan, or rating system in violation of this chapter is liable to the state for a civil penalty not to exceed five thousand dollars ($5,000) for each act, or if the act or practice was willful, a civil penalty not to exceed ten thousand dollars ($10,000) for each act.

Enforcement of Section 1858.07 is exclusively within in the authority of the Commisioner of Insurance. Subpart (b) of that section provides: "The penalty imposed by this section shall be imposed by and determined by the commissioner . . . ." The charging of unauthorized premiums is also prohibited by California's Insurance Unfair Practices Act which prohibits unfair methods of competition and unfair or deceptive acts and practices in the business of insurance.[2] Cal. Ins. Code § 790 *et seq.* The Insurance Unfair Practices Act itself states that it is intended to preempt federal law as permitted by the McCarran-Ferguson Act. Section 790 of the California Insurance Code provides:

> The purpose of this article is to regulate trade practices in the business of insurance in accordance with the intent of Congress as expresed in [the McCarran-Ferguson Act], by defining, or providing for the determination of, all such practices in this State, which constitute unfair methods of competition or

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[2] The Insurance Unfair Practices Act is applicable to insurance brokers such as Petitioners. Cal. Ins. Code § 790.01.

unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined.

Not only is there a comprehensive state regulatory scheme prohibiting the charging of excessive premiums, but those statutes have been construed by the California courts to preclude private causes of action under insurance and consumer protection statutes. In *Moradi-Shalal v. Fireman's Fund Insurance Co.*, 46 Cal.3d 287, 758 P.2d 58, 250 Cal. Rptr. 116 (1988), the California Supreme Court held that there was no private right of action under the Insurance Unfair Practices Act. Recently, the California Supreme Court stated that the Insurance Unfair Practices Act was enacted "to displace feedral law." *Manufacturers Life Insurance Company v. Weil Insurance Agency, Inc.*, 10 Cal.4th 257, 266, 275, 895 P.2d 56, 41 Cal.Rptr.2d 220 (1995). Thus, not only has the California legislature exhaustively regulated the practices at issue in this case, the California courts have repeatedly ruled that the insurance regulatory scheme created by the California legislature is intended to supersede any federal law that might otherwise have been applicable. A half century ago, Congress in enacting the McCarron-Ferguson Act granted state legislatures this power. Although Congress has never modified its stance, the Ninth Circuit now has significantly amended the McCarron-Ferguson Act by allowing federal remedies never contemplated in the California insurance regulatory statutes.

Amici believe that the Ninth Circuit erred in concluding that the availability of a civil RICO action will not impair California's comprehensive regulatory scheme which grants exclusive enforcement authority to the Commisioner of Insurance. The Ninth Circuit, in holding that McCarran-Ferguson's "impairment" language is not triggered by federal statutes which provide remedies significantly broader than those available under state insurance laws, in practical terms may have gutted the McCarran-Ferguson Act. Under the Ninth Circuit's in-

terpretation, only in the very rare instance when a federal statute of general application prohibits conduct allowed under state insurance law, or visa versa, will McCarran-Ferguson preemption apply.

The Ninth Circuit relied on the Seventh Circuit's decision in *NAACP v. American Family Mutual Insurance Co.*, 978 F.2d 287 (7th Cir. 1992), *cert. denied*, 113 S. Ct. 2335 (U.S. 1993), in reaching its decision in *Merchant Home Delivery*. Amici question whether *American Family Mutual* was correctly decided, since its conclusion that federal law is only preempted where there is a direct conflict between the substantive state and federal provisions is difficult to reconcile with other decisions construing the impairment language of the McCarran-Ferguson Act. *See, e.g., F.T.C. v. National Casualty Co.*, 357 U.S. 560 (1958) (federal false advertising statute preempted by state insurance false advertising statute based on the same model as California's Insurance Unfair Practices Act); *Gordon v. Ford Motor Credit Co.*, 868 F. Supp. 1191 (N.D. Cal. 1992) ("application of RICO would impair, invalidate and supersede the body of substantive laws which California has enacted to govern insurance practices"); *Wexco, Inc. v. IMC, Inc.*, 820 F. Supp. 194 (M.D. Pa. 1993) (McCarran-Ferguson preemption where insurance broker accepted premium but failed to secure insurance—the precise conduct alleged in *Merchant Home Delivery*). Nevertheless, the *Merchant Home Delivery* goes well beyond the decision in *American Family Mutual*. In *American Family Mutual*, the Seventh Circuit noted: "No official of Wisconsin has appeared in this litigation to say that a federal remedy under the Fair Housing Act would frustrate any state policy." *NAACP v. American Family Mutual, supra*, 978 F.2d at 297. In profound contrast, the California courts have explicitly stated that state insurance laws would be subverted and subsumed by the availability of a private RICO action for conduct in violation of insurance regulatory laws.

The Ninth Circuit's holding in *Merchant Home Delivery* is flatly contrary to a California appellate decision *explicitly* stating that the state's insurance regulatory policy would be subverted and subsumed by the availability of a private RICO action for conduct governed by the Insurance Unfair Practice Act and other provisions of the California Insurance Code granting exclusive enforcement authority to the Insurance Commissioner. *American International Group, Inc. v. Superior Court*, 234 Cal. App.3d 749, 285 Cal. Rptr. 765 (1991), *cert. denied sub nom. Brutoco Engineering & Construction, Inc. v. American International Group, Inc.*, 504 U.S. 911 (1992). In reaching this conclusion, the California Court of Appeal stated:

> Allowance of a RICO action seeking civil damages (including treble damages and attorney's fees) for the very conduct which California has chosen to regulate administratively would subvert and subsume the existing statutory scheme. It would permit a civil damage recovery where our Supreme Court has recently and explicitly held that none was intended. (*Moradi-Shalal, citation omitted.*) This would not be the first time creative litigation efforts had been unsuccesfully expended to get around that decision.

American International Group, Inc. v. Superior Court, supra, 234 Cal.App.3d at 768, 285 Cal. Rptr. at 777.

Remedies are not an inconsequential detail of California's system of regulating insurance practices. California's policy of limiting the remedies available to private parties for actions in violation of statutes regulating the conduct of insurers has been articulated in a series of recent decisions by the California courts. This history begins with *Royal Globe Insurance Co. v. Superior Court*, 23 Cal.3d 880, 592 P.2d 329, 153 Cal. Rptr. 842 (1979), in which the California Supreme Court held that a private plaintiff could bring an action for insurer practices in violation of the Insurance Unfair Practices Act (Cal. Ins. Code § 790 *et seq.*). Almost ten years later,

in *Moradi-Shalal, supra*, 758 P.2d 58, 46 Cal.3d 287, 250 Cal.Rptr. 116, the Supreme Court concluded *Royal Globe* had been incorrectly decided and eliminated private rights of action under the Insurance Unfair Practices Act.[3]

Amici are not jumping at shadows in believing that the *Merchant Home Delivery* decision carves a large hole in Congress' mandate that insurance be regulated by the states, rather than subject to federal statutes of general application. Since in *Merchant Home Delivery* there was a prior determination by a state court that the RICO remedies were incompatible with California's insurance regulatory statutes, it is unlikely that a federal statutory remedy can ever be found to "invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance" under the Ninth Circuit's interpretation of the McCarran-Ferguson Act.

Where a state has declared its policy of limiting the remedies available for violations of its insurance regulatory statutes as unequivocally as California has here, there is a direct and significant conflict between the state policy and a federal statute which allows not only a private right of action, but also treble damages and attorney's fees. Amici respectfully submit that the Ninth Circuit erred in concluding that there was no conflict between federal and state law is this case.

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[3] A subsequent series of decisions has held that the Insurance Unfair Practices Act preempts other state statutes under which a private right of action is available, if the alleged insurer misconduct is within the scope of the Insurance Unfair Practices Act. The California courts have been resistant to attempts to end-run the limitations on private actions imposed in *Moradi-Shalal*. *See, e.g., Maler v. Superior Court*, 220 Cal. App.3d 1592, 270 Cal. Rptr. 222 (1990); *Safeco Insurance Co. v. Superior Court*, 216 Cal. App.3d 1491, 265 Cal. Rptr. 585 (1990); *Industrial Indemnity Co. v. Superior Court*, 209 Cal. App.3d 1592, 257 Cal. Rptr. 1093 (1989).

B. The *Merchant Home Delivery* Decision Does Not Serve the Best Interests of Policyholders.

Amici firmly believe that fraudulent, unfair or deceptive acts against policyholders should not be tolerated. However, it does not follow that policyholders' welfare increases whenever an additional remedy is made available. The costs of defending policyholders against lawsuits brought by other parties and the cost of disputes concerning the extent of coverage under insurance policies are reflected in insurance premiums. *Merchant Home Delivery* opens the door to the practice of filing garden variety bad faith insurance claim settlement and insurance coverage disputes as RICO actions. The availability of treble damages and attorneys' fees is likely to make this opinion attractive to a large number of litigants.

There can be no doubt that insurance premiums will increase as cases are settled at higher figures because of the threat of RICO remedies. Insurers' ability to resist excessive or fraudulent claims will be undercut by the availability of private RICO actions with the potential for treble damages and attorneys' fees. Insurers are likely to settle inflated or dubious claims which formerly would have been contested more virogously. Policyholders will pay the price in higher premiums.

The use of RICO as the vehicle of choice for routine insurance litigation has several additional consequences. First, federal rather than state courts will increasingly be deciding insurance bad faith claim settlement and coverage cases. Not only will this impose an increased burden on the federal court system, it also is likely to result in unpredictable and inconsistent decisions. As happened in *Merchant Home Delivery*, a federal court may well reach a different conclusion than the state court on the availability of federal remedies. Moreover, the federal courts are divided on the application of RICO in insurance liti-

gation.[4] As a consequence, Amici's member companies who do business country-wide will face a different gamut of remedies in different jurisdictions, or between federal and state courts in the same jurisdiction. This unpredictability, in and of itself, will increase costs to Amici's member companies; cost which ultimately are passed along to policyholders.

Second, if the Ninth Circuit's decision in *Merchant Home Delivery* is allowed to stand, many aspects of insurance regulation which are peculiarly within the expertise of the various state insurance commissioners will be addressed in private litigation. Courts in contexts other than McCarran-Ferguson have wisely avoided intruding into matters subject to the approval of regulatory agencies. *See, e.g., Wegoland, Ltd. v. Nynex Corp.*, 27 F.3d 17, 21 (2d Cir. N.Y. 1994) (in a RICO action "that the remedy sought can be characterized as damages for fraud does not negate that fact that the court would be determining the reasonableness of rates"). For example, insurance commissioners routinely conduct "market conduct" examinations of insurers. Such examinations cover a wide range of marketing, underwriting and claims settlement practices. A market conduct examination culminates in a formal report setting forth areas in which the insurer's practices do not conform to the requirements of the state's statutes or regulations. Depending on the magnitude of the discrepancies uncovered in the examination, the insurance commissioner may merely instruct the insurer to take corrective action, or it may seek a consent decree with a substantial civil penalty.

Under *Merchant Home Delivery*, a policyholder or agent aggrieved by a practice criticized in a market conduct examination will have a ready-made cause of action under RICO. Disputes between insurers and insurance

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[4] See cases at footnote 4 in the Petition for Writ of Certiorari.

regulators concerning the content of market conduct examination reports and the recommended remedies will become common. Consent decrees will be entered into less frequently because insurers will no longer view entry of a consent decree and the payment of a penalty as closing an examination, but as opening the door to further litigation. As a consequence, the insurance regulator's enforcement resources will be stretched thin as the federal courts become the principal forum for regulating the conduct of insurance companies and their agents and employees.

Amici submit that the Ninth Circuit's conclusion that allowing a private RICO action for the overcharging of premiums on insurance policy would not impair a state regulatory scheme was incorrect. The California courts have explicitly stated that allowing private statutory remedies for activities governed by the Insurance Unfair Practices Act and other Insurance Code provisions would disrupt California's regulatory regime. Since the *Merchant Home Delivery* decision does not in any manner limit the varieties of alleged insurer misconduct which are now to be made subject to RICO, the incentives of treble damages and attorney's fees will increase the number of private claims filed against insurers and increase the cost of resolving those actions. The cost of this upsurge in litigation will be borne by insurers and their policyholders. Amici submit that the costs of adding RICO damages to state law remedies significantly outweigh any benefits to policyholders or the public.

II. THE NARROW DEFINITION OF "BUSINESS OF INSURANCE" ADOPTED BY THE NINTH CIRCUIT UNDULY LIMITS McCARRAN-FERGUSON.

The Ninth Circuit adopted an exceptionally narrow definition of "business of insurance" in the *Merchant Home Delivery* decision. This definition cannot be reconciled with the decisions of this Court regarding the scope

of the "business of insurance." The Court has enunciated a three part test for determining whether a practice falls within the "business of insurance": 1) whether the practice involves risk-spreading, 2) whether the practice is an integral part of the relationship between an insurer and an insured, and 3) whether the practice is limited to entities within the insurance industry. *United Labor Life Insurance Co. v. Pireno,* 458 U.S. 119, 129 (1982).

The Court has recently held that this test should be construed narrowly where an exemption from the antitrust laws is claimed and broadly in all other instances. *U.S. Department of the Treasury v. Fabe,* 113 S. Ct. 2202 (1993). In *Fabe,* the Supreme Court found that the Ohio insurer insolvency priority statute preempted federal law under McCarran-Ferguson. In so holding, the Supreme Court distinguished cases involving the narrow insurer exemption from antitrust liability and stated that the first clause of section 2(b) of the McCarran-Ferguson Act, 15 U.S.C.A. § 1012(b), "is not so narrowly circumscribed" as the second clause setting forth the antitrust exemption.[5] *Id.* at 2209. In *Fabe,* the Supreme Court stated that the first clause of section 2(b)—the portion of the McCarran-Ferguson Act at issue in this case—"was intended to further Congress' primary objective of granting the states *broad* regulatory authority over the business of insurance." *Id.* at 2210 (emphasis added).

The distinction drawn in *Fabe* between the narrow McCarran-Ferguson exemption from antitrust laws and the broad exemption from all other federal statutes cannot be reconciled with the Ninth Circuit's analysis of the

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[5] The first clause of section 2(b), which contains the "invalidate, impair or supersede" language is set forth above. The second clause provides: "After June 30, 1948, . . . the Sherman Act, . . . the Clayton Act, and the . . . Federal Trade Commission Act . . . shall be applicable to the business of insurance to the extent that such business is not regulated by the states.

"business of insurance." In holding that the failure of an insurance entity to deliver an insurance product while accepting premium is not within the "business of insurance," the Ninth Circuit applied an unduly narrow interpretation of this Court's three part test. Amici respectfully submit that the decision misconstrues the first (risk transfer) and second (insurer-insured relationship) parts of the test, while substantially ignoring the third (the practice is limited to the insurance industry) component. The Ninth Circuit concluded that because no insurance coverage was provided, there was no risk transfer and no insurer-insured relationship. *Merchant Home Delivery v. Hall & Co., supra*, 50 F.3d at 1490-1491. This analysis ignores the plain fact that the plaintiff in this case was attempting to transfer risk and intended to enter into an "insurer-insured" relationship.

The *Merchant Home Delivery* decision treats the individual insurance contracts which were not delivered as not being part of the "business of insurance," notwithstanding the stream of insurance policies purchased by Respondent through Petitioner insurance brokers. Only by disaggregating the insurer-insured relationship did the Ninth Circuit conclude that the failure to provide requested insurance coverage is not within the "business of insurance." This microscopic view of an ongoing relationship implies that many other transactions previously considered to be the "business of insurance" may not be subject to McCarran-Ferguson preemption. In particular, the *Merchant Home Delivery* decision cannot be reconciled with the recent Eleventh Circuit decision in *Barnett Bank of Marion County, N.A. v. Gallagher*, 43 F.3d 631 (11th Cir. 1995) *cert. granted*, No. 94-1837 (U.S. Sept. 27, 1995) which held that the McCarran-Ferguson exemption applies to *potential* as well as actual policyholders.[6] *Barnett* is consistent with this Court's decision in *F.T.C.*

[6] The Respondent indisputably was a potential policyholder with respect to the insurance coverage which allegedly was not provided.

v. National Casualty Co., 357 U.S. 560, 78 S. Ct. 1260 (1958). That decision held that the Federal Trade Commission had no authority to regulate advertising by insurers because such advertising was regulated by state insurance laws which, pursuant to the McCarran-Ferguson Act, preempted the federal statute. Advertising is directed to potential policyholders, and does not—in the microscopic view adopted in *Merchant Home Delivery*—involve either risk transfer or an existing insurer-insured relationship. Thus, the *Merchant Home Delivery* decision simply cannot be reconciled with this Court's established test for determining activities which constitute the "business of insurance."

Under the Ninth Circuit's *Merchant Home Delivery* analysis, every failure to provide insurance coverage could trigger a RICO claim on the theory that if no coverage was provided, no risk transfer took place. There are numerous disputes each year between policyholders and insurers concerning whether coverage for particular losses exists and whether the insurer (or its agent) misrepresented that such losses would be covered. Such disputes will be readily characterized as the provision of "sham insurance policies." *Merchant Home Delivery v. Hall & Co., supra,* 50 F.3d at 1491. If not overturned, the *Merchant Home Delivery* decision will permit policyholders and third party claimants to introduce a host of federal statutory allegations into coverage and sales misrepresentation cases. There can be little doubt that McCarran-Ferguson preemption will be eroded and that the number of suits involving insurance claims filed in federal courts is likely to explode.

CONCLUSION

For the reasons stated herein, Amici respectfully request that the Petition for Writ of Certiorari be granted.

Respectfully submitted,

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vs.

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Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF OF FARMERS INSURANCE EXCHANGE AND STATE FARM FIRE AND CASUALTY COMPANY AS AMICI CURIAE IN SUPPORT OF PETITIONERS

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No. 95-409

In The

Supreme Court of the United States

October Term, 1995

PROMETHEUS FUNDING CORP., etc., et al.,

Petitioners,

vs.

MERCHANTS HOME DELIVERY SERVICES, INC.,

Respondent.

On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit

BRIEF OF FARMERS INSURANCE EXCHANGE AND STATE FARM FIRE AND CASUALTY COMPANY AS AMICI CURIAE IN SUPPORT OF PETITIONERS

INTEREST OF THE AMICI CURIAE

Farmers Insurance Exchange ("Farmers") and State Farm Fire and Casualty Company ("State Farm") are insurance carriers conducting business in California and elsewhere. They have a vital interest in the issues presented by the pending petition for writ of certiorari. The Ninth Circuit's decision in this case threatens to expose Farmers, State Farm and all other insurers to greatly expanded liability under federal laws, liability to which insurers have not previously been exposed. Farmers and State Farm believe such expanded liability would translate into increased insurance costs, exacerbating already severe problems of insurance scarcity and unaffordability

to the serious detriment of both insurers and the insurance-buying public.

The parties have consented to the filing of amicus curiae briefs supporting and opposing the petition for writ of certiorari. Letters documenting the parties' consent are being submitted with this brief.

SUMMARY OF ARGUMENT

Section 2(a) of the McCarran-Ferguson Act ("the McCarran Act" or "the Act"), 15 U.S.C.A. § 1012(a) (West 1976), provides that the business of insurance shall be subject to the laws of the states relating to the regulation of that business. Section 2(b) of the Act then declares, in pertinent part: "No Act of Congress shall be construed to *invalidate, impair, or supersede* any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance." *Id.* § 1012(b) (emphasis added).

The Ninth Circuit has construed section 2(b) of the McCarran Act to permit a private action against an insurance broker under the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C.A. §§ 1961-1968 (West 1984 & Supp. 1995), based on conduct (overcharging for premiums) that is already strictly regulated by California's insurance laws. The Ninth Circuit held that, absent a *direct conflict*, a federal statute does not "invalidate, impair, or supersede" a state statute, even though the federal statute injects into the state scheme a new remedy the state legislature chose not to make available.

The Ninth Circuit's narrow reading of the McCarran Act is unfaithful to its language, which neither requires nor contemplates a direct conflict between state and federal law. Congress intended to leave the states with virtually plenary power to regulate the business of insurance unimpeded by general federal legislation not specifically targeted at that business. To effectuate this intent, Congress chose the broad phrase "invalidate,

impair, or supersede." Numerous courts have held a federal statute "impairs" state law even though not in direct conflict with such law if, as here, the federal statute introduces remedies not available under state law. The sole authority on which the Ninth Circuit relied, a 1992 decision by the Seventh Circuit, is unpersuasive because that court started from the *premise* that the McCarran Act requires a direct conflict between state and federal law yet cited no authority for the proposition and failed to explain how it derived such a rule from the text of the Act. One district court recently criticized the decisions of both the Seventh and Ninth Circuits on this and other grounds.

The Ninth Circuit's erroneous reading of the McCarran Act will seriously disrupt the insurance markets in California and possibly elsewhere. The California courts have warned that permitting a private action against insurers under RICO based on conduct that is already comprehensively regulated by state law will seriously upset the state regulatory scheme. Heedless of this warning, the Ninth Circuit has construed the McCarran Act virtually out of existence in RICO cases. Henceforth, not only overcharging for premiums but virtually any insurer misdeed regulated by state law may support a RICO claim. To subject insurers to RICO's threat of treble damages and attorney fees, threats they do not face under state law, cannot help but disrupt the insurance market by increasing the cost of insurance. Meritorious or not, the mere presence of a RICO claim in a suit against an insurer will have an extortionary effect and will coerce settlement of many claims insurers otherwise would have successfully defended. In this era of insurance scarcity and unaffordability, insurers and the insurance-buying public are profoundly disserved by a judicial decision that unjustifiably subjects insurers to greatly expanded liability and costs.

ARGUMENT

THIS COURT SHOULD GRANT THE PETITION FOR WRIT OF CERTIORARI BECAUSE THE NINTH CIRCUIT'S NARROW READING OF THE MCCARRAN-FERGUSON ACT IS ERRONEOUS AND DISRUPTIVE.

A. The Ninth Circuit's Reading Of The Act Is Unfaithful To Its Language, Which Does Not Require Or Contemplate A Direct Conflict Between State And Federal Law.

Prior to this Court's decision in *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), "it had been assumed that '[i]ssuing a policy of insurance is not a transaction of commerce,' . . . subject to federal regulation. Accordingly, 'the States enjoyed a virtually exclusive domain over the insurance industry.' " *U.S. Dep't of Treasury v. Fabe*, 113 S. Ct. 2202, 2207 (1993) (citation omitted). In *South-Eastern Underwriters*, the Court held the insurance business was indeed engaged in interstate commerce and was therefore subject to federal regulation. "This result, naturally, was widely perceived as a threat to state power to tax and regulate the insurance industry. To allay those fears, Congress moved quickly to restore the supremacy of the States in the realm of insurance regulation. It enacted the McCarran-Ferguson Act within a year of the decision in *South-Eastern Underwriters*." *Id.*

"[T]he primary purpose of the McCarran-Ferguson Act was to preserve state regulation of the activities of insurance companies, as it existed before the *South-Eastern Underwriters* case." *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 218 n.18 (1979) (emphasis omitted). Congress declared "that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States." 15 U.S.C.A. § 1011 (West 1976).

To effectuate this policy, the McCarran Act provides:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
>
> (b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance . . . .

Id. § 1012.

Thus, the McCarran Act bars application of a federal statute to the business of insurance where: (1) the statute does not specifically relate to the business of insurance; (2) the acts challenged under the statute constitute the business of insurance; (3) the state has enacted a law or laws regulating the challenged acts; and (4) the state law would be superseded, impaired or invalidated by the application of the federal statute. *Cochran v. Paco, Inc.*, 606 F.2d 460, 464 (5th Cir. 1979).

The parties here do not dispute that the first and third prongs of this four-part test were satisfied with respect to all the practices challenged by plaintiff's complaint. *Merchants Home Delivery Serv., Inc. v. Frank B. Hall & Co.*, 50 F.3d 1486, 1489 (9th Cir. 1995). Moreover, the court of appeals had no difficulty holding the second prong was satisfied with respect to the defendants' alleged practice of "[o]vercharging for premiums on actual [insurance] policies." *Id.* at 1490. The court rightly viewed this type of transaction to be "at the core of the 'business of insurance.' " *Id.*

Thus, whether the McCarran Act permitted plaintiff to maintain an action under RICO challenging defendants' alleged practice of overcharging for existing policies turned on the fourth prong of the four-part test – whether application of RICO would "invalidate, impair, or supersede" California's comprehensive regulatory scheme.

In answering this question, the Ninth Circuit adopted an exceedingly narrow construction of the language of the McCarran Act. The court held that, absent a *direct conflict*, a federal statute does not "invalidate, impair, or supersede" a state statute even though the federal statute injects into the state scheme new remedies the state legislature chose not to make available. In the court's view, "the application of a federal statute prohibiting acts which are also prohibited under a state's insurance laws does not 'invalidate, impair, or supersede' the state's laws under § 2(b) of the McCarran-Ferguson Act." *Id.* at 1492. The court concluded: "Under this rule, § 2(b) allows the application of RICO to the present facts. Hall concedes . . . that California law prohibits the acts alleged by Merchants. As RICO prohibits these same acts, there is no conflict; RICO does not invalidate, impair, or supersede California law in this context." *Id.*

The Ninth Circuit's reading of the McCarran Act is flawed as a matter of statutory construction. This Court has explained "the starting point in a case involving construction of the McCarran-Ferguson Act, like the starting point in any case involving the meaning of a statute, is the language of the statute itself." *Group Life & Health Ins. Co.*, 440 U.S. at 210. The Act provides: "No Act of Congress shall be construed to *invalidate, impair, or supersede* any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance: . . . . " 15 U.S.C.A. § 1012(b) (emphasis added).

"The words 'invalidate, impair and supersede' are not defined in the McCarran-Ferguson Act[,]" so they "must be given their ordinary meaning unless another meaning is dictated by the context in which they are used." *Ambrose v. Blue Cross & Blue Shield of Virginia, Inc.*, 891 F. Supp. 1153, 1165 (E.D. Va. 1995). Context dictates no extraordinary meaning in this case.

" 'Invalidate' means to 'weaken or make valueless' or to discredit. It is a synonym for nullify. 'Impair' means to

'make worse . . . diminish in quantity, value, excellence or strength . . . do harm to.' " *Id.* (quoting Webster's Third New International Dictionary 1131, 1188 (1986) (alteration in original)); *see Brownell v. State Farm Mut. Ins. Co.*, 757 F. Supp. 526, 536 n.13 (E.D. Pa. 1991) (citing Webster's Ninth New Collegiate Dictionary 603 (1986) and Webster's Collegiate Thesaurus 418 (1976)) (As used in the McCarran Act, " '[i]mpair' means to damage, injure, diminish, prejudice, undermine or weaken."). " 'Supersede' means to 'make obsolete, inferior, or outmoded . . . to make void . . . to make superfluous or unnecessary.' " *Ambrose*, 891 F. Supp. at 1165 (quoting Webster's Third New International Dictionary, *supra*, at 2295).

Given these definitions, it is clear a federal statute can "invalidate, impair and supersede" state regulations without directly conflicting with them. Where a state has enacted a comprehensive, detailed statutory and regulatory scheme governing the business of insurance, including a carefully crafted system of enforcement and penalties for unfair or deceptive practices, to allow a plaintiff to invoke a federal statute and seek a remedy not available under the state scheme is to diminish, undermine, weaken, and nullify the state's authority.

Had Congress intended the McCarran Act to receive the narrow reading the Ninth Circuit accorded it, Congress would have employed the word "conflict" rather than the phrase "invalidate, impair, or supersede." Congress chose the latter, more sweeping phrase because Congress intended the states to have virtually plenary power to regulate the business of insurance unimpeded by general federal legislation not specifically targeted at that business. (*See* Petition for Writ of Certiorari at 8-10.)

B. The Ninth Circuit's Reading Of The Act Is Contrary To Numerous Cases.

Consistent with the plain language of the McCarran Act, numerous courts have held the Act bars a RICO

claim based on insurance practices regulated by state law where recovery under RICO would undermine, disrupt, upset or simply alter the remedial scheme established by the state legislature. These courts do not read the McCarran Act to require a direct conflict between state and federal law.

For example, in *Senich v. Transamerica Premier Insurance Co.*, 766 F. Supp. 339 (W.D. Pa. 1990), the plaintiffs filed an action against certain insurers under RICO alleging, as plaintiff did here, "that their premiums were excessive." *Id.* at 341. Noting that Pennsylvania had enacted "comprehensive laws which regulate the business of insurance," *id.* at 340, including laws governing the fixing of premiums, the court held the McCarran Act barred plaintiffs' RICO claim:

> Pennsylvania has enacted the Casualty and Surety Rate Regulation Act ("Rate Act"), . . . which provides that '[r]ates shall not be excessive' and requires insurance companies to gain approval from the Pennsylvania Department of Insurance for their proposed premium rates. . . . In addition, the Rate Act provides for an administrative procedure whereby persons 'aggrieved with respect to any filing which is in effect' may file complaints with the Insurance Commissioner and have a hearing. . . . *[S]ince Pennsylvania insurance law extensively regulates the fixing of such rates, Plaintiffs' RICO claims, under which they characterize their premium grievances, would 'invalidate, impair, or super[s]ede' the state's laws.*

Id. at 341 (emphasis added) (citations omitted). The court observed that, "while alleging RICO violations, the plaintiffs are attempting to reach the defendants' underlying insurance practices which are subject to the comprehensive Pennsylvania regulatory scheme." *Id.* at 342. The McCarran Act barred such an attempt.

Likewise, in *LeDuc v. Kentucky Central Life Insurance Co.*, 814 F. Supp. 820 (N.D. Cal. 1992), certain agents for a

life insurer filed actions against the insurer under RICO alleging the insurer "engaged in a pattern of making false and fraudulent representations to its agents, and to members of the general public in order to perpetrate a scheme that would allow [the insurer] to distort its financial condition so that its agents would be induced to sell, and members of the general public would be induced to purchase," the insurer's policies and annuity investments. *Id.* at 827. The court granted the insurer's motion to dismiss the RICO claim. To permit plaintiffs to proceed under RICO, the court reasoned, would "impair" and "supersede" California's comprehensive statutory and regulatory scheme governing unfair and deceptive insurance practices by introducing new remedies not available under state law:

> The application of a federal statute to matters regulated by state insurance law would arguably impair state law. For instance, RICO violations include treble damages and attorneys' fees. The California legislature has not provided such remedies for misrepresentations regarding an insurance company's financial condition. In fact, applying RICO would nullify the state's determination of the appropriate remedies for certain conduct and would supersede remedies and regulatory supervision provided by California law.

Id. at 829. Like the *Senich* court, the *LeDuc* court did not require a showing that RICO directly conflicted with any state law. The McCarran Act applied because "California's comprehensive regulatory supervision of insurers' financial conditions would be *undermined and disrupted* if agents and policyholders were permitted to assert federal RICO claims based upon allegations of financial nondisclosure." *Id.* (emphasis added).

To the same effect is *Wexco Inc. v. IMC, Inc.*, 820 F. Supp. 194 (M.D. Pa. 1993). The court ruled the McCarran Act barred plaintiffs from proceeding under RICO based on insurance practices regulated by state law, not because

RICO *conflicted* with state law but because RICO's remedial scheme *differed* from, and thus disrupted, the comprehensive scheme the state legislature had enacted:

> [T]he Pennsylvania legislature chose to have [the Pennsylvania Unfair Insurance Practices Act] and other Pennsylvania insurance regulatory law enforced solely by the Commonwealth's Insurance Commissioner. There is no private cause of action available for violation of the PUIPA or any Pennsylvania insurance regulations. . . . While Pennsylvania courts have held that common law causes of action available prior to the enactment of the PUIPA, such as common law fraud and deceit actions, continue to be viable options for aggrieved insureds, . . . such common law actions do not reward plaintiffs with the treble damages, costs and attorney fees mandated by RICO. . . . The availability of a federal private action under RICO would not merely nullify the state's chosen regulatory remedies for insurance entity misconduct. Rather, this court believes that the availability of a federal private remedy which would reward successful business plaintiffs, such as the captioned parties, with treble damages, costs and attorney fees cannot help but upset the balance of relationships between insurance entities and insureds which are established and regulated by PUIPA and the other state laws . . . .

Id. at 203-04 (footnotes and citations omitted).

The court followed *LeDuc* and *Wexco* in *Forsyth v. Humana, Inc.*, 827 F. Supp. 1498 (D. Nev. 1993). The court reasoned that, because the state did not regulate the challenged unfair insurance practices with "the same harsh penalties which would be available under RICO[,]" *id.* at 1521, application of RICO would impair state law: "For this Court to allow Plaintiffs to pursue the harsher

RICO penalties for behavior which the Nevada Legislature apparently did not deem worthy of such penalties, would be tantamount to allowing Congress to intercede in an area expressly left to the states under the McCarran-Ferguson Act." *Id.* at 1521-22.

Yet again, in *Everson v. Blue Cross & Blue Shield*, No. 93CV7534, 1994 WL 675200 (N.D. Ohio June 15, 1994), the court held RICO's provision of treble damages and attorney fees would impair a state regulatory scheme which afforded no private right of action: "The Ohio legislature has chosen to have Ohio insurance regulatory law enforced solely by the Superintendent of Insurance. There is no private cause of action . . . . Thus, application of RICO would impair the enforcement of Ohio insurance law." *Id.* at *12 (citation omitted). The *Everson* court rejected the argument that RICO cannot be said to impair state law when that law affords a right of action for fraud: "Plaintiffs argue . . . that because private actions for common law fraud exist in addition to actions under § 3901.21 [regulating unfair and deceptive acts of insurance companies], a fraud-based RICO claim does not impair Ohio law. However, common law fraud actions 'do not reward plaintiffs with the treble damages, costs, and attorney fees mandated by RICO.' " *Id.*

Most recently, the district court for the Eastern District of Virginia likewise held that to permit private actions under RICO against insurers "would invalidate and impair the regulation sought to be accomplished" by Virginia's Unfair Trade Practices Act. *Ambrose*, 891 F. Supp. at 1165. The court explained that the threat of private litigation under RICO would undermine the state regulatory scheme by inhibiting insurers from settling disputes in the administrative setting:

> Most aggrieved insureds would opt for the prospect of treble damages [under RICO] rather than participate in remedial measures structured by [Virginia's State Corporation Commission, or "SCC"]. This would make insurers less willing to agree with the SCC to settle disputes over

> alleged violations for fear of compromising their positions in pending or threatened RICO litigation. The ability to act promptly and to secure for insureds settlements is central to the state's ability to protect insureds and to regulate the insured-insurer relationship.

Id. For these reasons, "[t]he prospect of treble damages and attorneys fees would weaken, diminish and do serious injury to, if not nullify, the sections of [the Unfair Trade Practices Act], and the enforcement mechanisms which protect and regulate that [insured-insurer] relationship." *Id.*

The *Ambrose* court further explained how, if private actions under RICO were available, RICO would supersede Virginia's laws:

> Because RICO provides for a private cause of action and treble damages, and because these provisions of RICO differ dramatically from the way in which Virginia's insurance code addresses the same conduct, RICO would in effect replace [the Unfair Trade Practices Act] as the principal means by which to remedy such conduct. It would convert a system of public redress into a system of private redress. The forum for redress would shift from the SCC to the federal courts.

Id.; *accord Richhart v. Metropolitan Life Ins. Co.*, Civ. A. No. 89-1725, 1990 WL 39268, at *3 (E.D. Pa. Mar. 30, 1990) (rejecting argument that RICO claim was merely "supplemental to the existing state regulatory scheme").

The parties here do not dispute that California "has enacted comprehensive legislation expressly designed to regulate the business of insurance," *American Int'l Group, Inc. v. Superior Court*, 285 Cal. Rptr. 765, 774 (Cal. Ct. App. 1991), *cert. denied*, 504 U.S. 911 (1992), *see* Cal. Ins. Code §§ 790-790.10 (West 1993 & Supp. 1995), including the practices of which respondent complained. *See Merchants Home Delivery Serv., Inc.*, 50 F.3d at 1489 & n.1.

Indeed, California's Unfair Practices Act was enacted specifically to invoke the protection of the McCarran Act. It was designed "to regulate trade practices in the business of insurance in accordance with the intent of Congress as expressed in the [McCarran Act] . . . by defining, or providing for the determination of, all such practices in this State which constitute . . . unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined." Cal. Ins. Code § 790 (West 1993).

The California legislature has charged the Commissioner of Insurance with the exclusive authority to enforce these laws; private actions for damages are not permitted. *Moradi-Shalal v. Fireman's Fund Ins. Cos.*, 758 P.2d 58, 65, 250 Cal. Rptr. 116, 123 (Cal. 1988); *Gordon v. Ford Motor Credit Co.*, 868 F. Supp. 1191, 1196 (N.D. Cal. 1992). For this reason, in addition to the court in *LeDuc* which is discussed above, at least two other courts have held the McCarran Act bars private actions under RICO based on practices that are regulated by California's comprehensive insurance law. *See Gordon*, 868 F. Supp. at 1196-97 (" 'California has enacted comprehensive legislation expressly designed to regulate the business of insurance.' . . . Investigatory and enforcement authority for violations of the Code have been delegated to the commissioner of insurance. . . . [G]iven California's extensive regulation of the insurance industry, this court concludes that application of RICO would impair, invalidate, and supersede the body of substantive laws which California has enacted to govern insurance practices in this state.") (citations omitted); *American Int'l Group, Inc.*, 285 Cal. Rptr. at 777 ("Allowance of a RICO action seeking civil damages (including treble damages and attorneys fees) for the very conduct which California has chosen to regulate administratively would subvert and subsume the existing statutory scheme. It would permit a civil damage

recovery where our Supreme Court has recently and explicitly held that none was intended.").[1]

In sum, the Ninth Circuit's reading of the Act cannot be squared with numerous well-reasoned decisions by other courts.

C. The Ninth Circuit's Reliance On *American Family Mutual* Was Misplaced. That Decision Was Poorly Reasoned And Has Been Justifiably Criticized.

The authority discussed above is compelling, yet the Ninth Circuit chose not to follow it. Instead, the court relied solely on the Seventh Circuit's decision in *NAACP v. American Family Mutual Insurance Co.*, 978 F.2d 287 (7th Cir. 1992), *cert. denied*, 113 S. Ct. 2335 (1993). The plaintiffs there filed an action against a property and casualty insurer alleging that the insurer practiced "redlining" and that the practice was a form of racial discrimination forbidden by the Fair Housing Act, 42 U.S.C.A. §§ 3601-3619 (West 1994). One of the issues before the

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[1] In *Moradi-Shalal*, 758 P.2d at 65, 250 Cal. Rptr. at 123, the California Supreme Court held California's Unfair Practices Act, Cal. Ins. Code § 790.03 (West 1993), affords no private right of action for damages against an insurer. The court grounded its decision on legislative intent, explaining section 790.03 was enacted to empower the Insurance Commissioner to police insurance company misconduct, not to create private rights of action. *Moradi-Shalal*, 758 P.2d at 65, 250 Cal. Rptr. at 123. In the Ninth Circuit, respondent's supporters dismissed the importance of *Moradi-Shalal*, noting the decision did not purport to limit common law causes of action against insurers. (Brief Of Amicus Curiae California Association Of Hospitals And Health Systems In Opposition To Appellees' Petition For Rehearing And Suggestion For Rehearing En Banc at 14-15.) However, at least two courts have rejected this very argument on the ground "common law actions do not reward plaintiffs with the treble damages, costs and attorney fees mandated by RICO." *Wexco Inc.*, 820 F. Supp. at 204; *accord Everson*, 1994 WL 675200 at *12.

court of appeals was whether the McCarran Act barred plaintiffs' claim. The court declared the insurer was required "to show that the Fair Housing Act conflicts with state law. Duplication is not conflict." *American Family Mutual*, 978 F.2d at 295. The court cited no authority for the proposition, nor did it explain how it derived such a rule from the text of the McCarran Act.

Viewing the McCarran Act as "a form of inverse preemption," *id.* at 296, the court stated "principles defining when state remedies *conflict with* (and so are preempted by) federal law are pertinent in deciding when federal rules 'invalidate, impair, or supersede' state rules." *Id.* (emphasis added). The court thus started from the premise that the McCarran Act requires a conflict between state and federal law, yet that was the very issue the court purported to decide.

The court proceeded to consider parallel state-federal regulations in various areas and concluded "state and federal rules that are substantively identical but differ in penalty do not conflict with or displace each other." *Id.* at 297. This conclusion begs the question, which is whether the McCarran Act requires that the federal statute "conflict with or displace" the state statute, or merely requires, as the many cases cited above have held, that the federal statute alter the remedial scheme established by the state.

In *Ambrose*, 891 F. Supp. 1153, the court provided a detailed and compelling critique of the Seventh Circuit's decision in *American Family Mutual* and the Ninth Circuit's decision in the present case. The *Ambrose* court rejected as "overly broad and inconsistent with the plain meaning of the language of Section 2(b)" the Seventh Circuit's unexamined premise and the Ninth Circuit's holding that "any federal statute which proscribes the same conduct as a state statute will never 'invalidate, impair or supersede' the state statute." *Id.* at 1166. The *Ambrose* court reasoned:

> First, the inquiry that the McCarran-Ferguson Act requires, whether federal law 'invalidate[s],

> impair[s], or supersede[s]' state law, does not lend itself to a blanket rule that certain types of inconsistencies can never satisfy that language. Rather, the language of Section 2(b) requires that a court look at the actual effect of the federal law on the specific state law. In this case, the court is persuaded that allowing claims under RICO will greatly impair the [State Corporation Commission's] ability to enforce Virginia's insurance code and, specifically, to secure from insurers settlements that are in the interest of all insureds and in the public interest as well. The court also finds the disparity between the cause of action and remedy permitted by RICO and the enforcement mechanism and remedy permitted by Virginia's insurance code to be so great that the federal law would in fact supersede the state law. To ignore these conclusions in favor of a bright line rule that no federal law can 'invalidate, impair, or supersede' a state law so long as they prohibit the same acts is contrary to the purposes of the McCarran-Ferguson Act as well as to its plain language.

Id. at 1166-67.

The *Ambrose* court further rejected the proposition that "federal and state laws that prohibit the same conduct 'but differ in penalty do not conflict with or displace each other.' " *Id.* at 1167 (quoting *American Family Mutual*, 978 F.2d at 297). The court observed:

> Virtually any state statute includes more than a simple proscription of conduct. It includes the appropriate penalty for that conduct and the appropriate mechanism for enforcing the proscription. A state law that prohibits an act, punishes it with a specific range of fines, makes it the subject of remedial action, and vests enforcement in a state quasi-judicial entity cannot be said to be consistent with a federal law that prohibits the same act, permits treble damages,

> fees, and costs, and expressly creates a personal cause of action.

Id.

Finally, the *Ambrose* court criticized the "flawed, analytical model" common to *American Family Mutual* and the Ninth Circuit's decision here, namely, construing the "invalidate, impair, or supersede" clause of the McCarran Act under the rubric of " 'inverse preemption.' " *Id.* The court explained that, unlike preemption analysis which turns on "status, *i.e.*, supremacy of a body of [federal] law," *id.*, the McCarran Act turns on "the effect of the law, *i.e.*, whether an act of Congress 'invalidates, impairs or supersedes' certain kinds of state law." *Id.* "Forcing the McCarran-Ferguson Act analysis into the preemption model distorts the analysis required by the statutory test fixed by the McCarran-Ferguson Act." *Id.* The court observed the improper use of preemption analysis led the Seventh and Ninth Circuits mistakenly to interpret the Act "to require a showing of direct conflict between the state and federal law" and to "conclud[e] that state and federal law could co-exist even though the federal law provided a cause of action not provided under state law and remedies greater than those provided by state law." *Id.*

In short, the reasoning of *American Family Mutual*, which the Ninth Circuit adopted in this case, is seriously flawed. Neither decision provides analytically sound support for the proposition that the phrase "invalidate, impair, or supersede" in the McCarran Act requires a direct conflict between state and federal law. This Court should take the opportunity presented by this case to settle this important issue by holding the McCarran Act does not require a direct conflict. As we explain in our concluding section below, the Ninth Circuit's decision, if left uncorrected, threatens serious consequences.

D. The Ninth Circuit's Reading Of The Act Will Seriously Disrupt The Insurance Markets In California And Possibly Elsewhere.

Aside from its legal deficiencies, the Ninth Circuit's reading of the McCarran Act is flawed as a matter of public policy. The California courts have warned about "the significant impact which the availability of a civil RICO claim would have upon California litigation between insurers and insureds given existing California decisional and statutory law." *American Int'l Group, Inc.*, 285 Cal. Rptr. at 768. Heedless of this warning, the Ninth Circuit has construed the McCarran Act so narrowly that not only overcharging for premiums but virtually any alleged insurer misconduct regulated by state law may henceforth support a RICO claim.

The court of appeals seemingly embraced respondent's construction of the McCarran Act, under which "application of a federal law would be precluded only where the federal law expressly prohibited acts permitted by state law, or vice versa." *Merchants Home Delivery Serv., Inc.*, 50 F.3d at 1492. When will this test ever be satisfied? Plaintiffs do not sue insurers for acts *permitted* by state law; they sue for acts prohibited by state law. RICO will rarely if ever conflict with such state law and, as construed by the Ninth Circuit, the McCarran Act will rarely if ever apply. The court effectively construed the Act out of existence in RICO cases.

In recent years, California insurance markets have been plagued by problems of scarcity and unaffordability.[2] To subject insurers to RICO's threat of treble

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[2] In the automobile insurance market, California drivers already face the nation's highest costs. *Retroactive Liability: Beyond Superfund?*, Facts & Trends (RAND/Institute for Civil Justice, Santa Monica, Cal.), Spring 1993, at 3, 4. "Large numbers of uninsured motorists are opting out of the system altogether." *Auto Insurance Reform: Soon or Never?*, Facts & Trends (RAND/

damages and attorney fees, threats they do not face under state law, cannot help but further disrupt the markets by increasing the cost of insurance. Meritorious or not, the mere presence of a RICO claim in a suit against an insurer will prompt settlement of many claims insurers otherwise would have successfully defended. As Justice Marshall observed, private civil litigants, "lured by the prospect of treble damages and attorney's fees, have a strong incentive to invoke RICO's provisions whenever they can allege in good faith two instances of mail or wire fraud. Then the defendant, facing a tremendous financial exposure in addition to the threat of being labeled a 'racketeer,' will have a strong interest in settling the dispute." *Sedima, S. P. R. L. v. Imrex Co.*, 473 U.S. 479, 504 (1985) (Marshall, J., dissenting).

Amici curiae supporting respondent have denied that exposing insurers to liability for treble damages and attorney fees under RICO will disrupt California's insurance markets. They have argued: "California allows punitive damages to be awarded against insurance companies that engage in fraudulent or malicious conduct. There is no reason to believe RICO's civil remedies are more 'disruptive' to the market than open-ended exposure to punitive damages." (Brief Of Amicus Curiae California

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Institute for Civil Justice, Santa Monica, Cal.), Winter 1993, at 1. In the homeowners insurance market, California is experiencing a "full-blown . . . coverage crisis that is threatening to cripple the state's slowly recovering economy." *Editorial Comment, A Bold Response to California Crisis*, National Underwriter, Aug. 14, 1995, at 28. Battered by the January 1994 earthquake near Los Angeles and faced with a state requirement that they offer earthquake coverage as part of every homeowners policy, more than 90 percent of the insurers formerly offering such policies have simply abandoned the California market. *Quackenbush Quake Plan No Slam Dunk in Legislature*, National Underwriter, Sept. 4, 1995, at 2; *California Insurers Praise Quackenbush's Quake Plan*, National Underwriter, Aug. 7, 1995, at 5, 24.

Association Of Hospitals And Health Systems In Opposition To Appellees' Petition For Rehearing And Suggestion For Rehearing En Banc at 9 n.8 (citation omitted).)

This reasoning is flawed. Punitive damages are restricted to cases where the plaintiff proves by *"clear and convincing evidence"* that the defendant "has been guilty of oppression, fraud, or malice . . . . " Cal. Civ. Code § 3294(a) (West Supp. 1995) (emphasis added). Moreover, the amount of punitive damages must bear a reasonable relationship to the plaintiff's compensatory damages and cannot exceed the defendant's ability to pay in light of its financial condition. *See Adams v. Murakami*, 813 P.2d 1348, 1350-52, 284 Cal. Rptr. 318, 320-22 (Cal. 1991); *Neal v. Farmers Ins. Exch.*, 582 P.2d 980, 990, 148 Cal. Rptr. 389, 399 (Cal. 1978). No comparable restrictions limit the damages and fees recoverable under RICO.

Further, the argument of respondent's supporters simply makes no sense. Regardless of insurers' exposure to punitive damages, the *added* exposure to civil remedies under RICO cannot help but increase insurers' costs and aggravate current problems in the insurance markets.

CONCLUSION

The Ninth Circuit's decision, which subjects insurers to greatly expanded liability and costs, is flawed as a matter of law and as a matter of public policy. It threatens a serious disruption of state insurance markets. For these reasons and those advanced by petitioners, this Court should grant the petition for writ of certiorari.

Respectfully submitted October 3, 1995

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Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

PROMETHEUS FUNDING CORP., etc., et al.,
Petitioners,

v.

MERCHANTS HOME DELIVERY SERVICES, INC.,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF AMICUS CURIAE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS SUPPORTING RESPONDENT

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BRIEF OF AMICUS CURIAE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS IN OPPOSITION TO PETITION FOR CERTIORARI

Petitioners and their *amici* contend that allowing persons injured in their business or property by a violation of the Racketeer Influenced and Corrupt Organizations Act ("RICO") that involves insurance, to bring suit under that Act would "impair" the enforcement of the California Insurance Code. The National Association of Insurance Commissioners ("NAIC"), whose members are the principal state insurance regulators, strenuously disagrees with the notion that RICO impairs any state's insurance laws. The NAIC urges, to the contrary, that RICO enhances the effective enforcement of those laws. Thus, the NAIC intervened as *amicus* in support of the Respondent in the Court of Appeals. It does so again here by consent of both parties in order unequivocally to apprise the Court that the NAIC opposes the petition for certiorari.

INTEREST OF THE AMICUS CURIAE

The NAIC is an association made up of the officials principally responsible for the regulation of insurance in all 50 states, the District of Columbia, and the territories and insular possessions of the United States. It strives to educate regulators and the industry, to eliminate conflicts between states, to advance uniformity of regulations where appropriate, and to sponsor and support activities that further effective enforcement of insurance laws.

One of the NAIC's most important roles is the promulgation of "Model Acts" for adoption by the various states, governing various aspects of the regulation of insurance. These documents are drafted through a consultative process among industry members, consumers, and regulators meant to develop consensus, eliminate technical problems, and ensure that the resulting law can be widely and uniformly adopted. California's Unfair Insurance Practices Act (UIPA) (Cal. Ins. Code § 790, *et seq.*) is substantially derived from the NAIC's Unfair Trade Practices Model Act.[1] The NAIC, then, is uniquely well-suited to inform this Court concerning the purposes and intent of the statute in question, and intensely interested in its proper interpretation.

In addition, the NAIC is deeply involved in helping its members fight insurance fraud and deceptive practices. The NAIC maintains a database of information about dubious characters involved in the insurance industry, supplies regulators with technical assistance and practical advice about fighting fraud, and works with the FBI, the Department of Labor, and other federal offices in anti-fraud activities. NAIC members themselves have made fruitful use of RICO to pursue the perpetrators of insurance fraud and the compensation of their victims in situations where the members were vested with the claims of defrauded insolvent insurers.[2] NAIC members have often

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[1] The 1972 text of the Unfair Trade Practices Model Act, which closely resembles the UIPA, is reprinted in the Appendix.

[2] Examples of such efforts which have resulted in (continued...)

supported and cooperated in federal criminal prosecutions of insurance fraudfeasors.[3]

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[2] (...continued)
published opinions include *Kempe v. Monitor Intermediaries, Inc.*, 785 F.2d 1443 (9th Cir. 1986); *Schacht v. Brown*, 711 F.2d 1343 (7th Cir.), *cert. denied*, 464 U.S. 1002 (1983); *In Re Diamond Benefits Life Insurance Co. and American Universal Insurance Co. Contracts Litigation*, M.D.L. No. 972 (D.Ariz. March 27, 1995) (Strand, J.); *Clark v. Milam*, 847 F. Supp. 409 (S.D.W.Va. 1994); *Durish v. Uselton*, 763 F. Supp. 192 (N.D.Tex. 1990); *State of North Carolina ex rel. Long v. Alexander & Alexander Services, Inc.*, 680 F. Supp. 746 (E.D.N.C. 1988). No RICO case brought by an insurance liquidator has ever been dismissed on McCarran Ferguson grounds.

[3] That federal prosecution of insurance charlatans for mail or wire fraud does not "impair" the state regulation of insurance was established in *United States v. Sylvanus*, 192 F.2d 96 (7th Cir.1951), *cert. denied*, 342 U.S. 943 (1952). Other examples of such prosecutions include *United States v. Cosentino*, 869 F.2d 301 (7th Cir.), *cert. denied*, 492 U.S. 908 (1989) (siphoning off insurance company assets through affiliated broker); *United States v. Joyce*, 499 F.2d 9 (7th Cir.), *cert. denied*, 419 U.S. 1031 (1974) (embezzlement of premium dollars from undercapitalized insurer); *United States v. Kreimer*, 609 F.2d 126 (5th Cir. 1980) (fraud against insurance company by agents, who accepted secret fees and commissions); and *United States v. Ferrell Travis Riley, et al.*, No. 94-00197-01/03-LR-W-8, Mealey's Insurance Insolvency Reporter, December 14, 1994 at 16 (W.D. Mo. 1994) (bribery of insurance (continued...)

The unfortunate fact is that insurance lends itself all too readily to fraud. As the House Committee on Energy and Commerce explained:

> The business of insurance is uniquely suited to abuse by mismanagement and fraud. Making believable promises is a stock item in every con man's bag of tricks. The prepayment of large, often vast, sums of money with few restrictions lends itself naturally to monumental wasting of assets through greed, incompetence, and dereliction of duty. This combination of easy money based on easy promises makes the insurance industry an irresistible target for financial knaves and buccaneers.

Staff of House Committee on Energy and Commerce, 101st Cong. 2d Sess., "Failed Promises: Insurance Company Insolvencies" (Comm. Print 101-P 1990).

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[3] (...continued)
commissioners and false reporting on financial statements). *United States v. Miro*, 29 F.3d 194 (5th Cir. 1994) involved the mail fraud conviction of a fraudfeasor who caused losses conservatively estimated at $20 million, by means of United States and foreign insurance companies.

Recently, a criminal RICO action has snared the notorious Alan Teale. *United States v. Alan Teale, et al.*, No. 93-00002, Mealey's Insurance Insolvency Reporter, August 18, 1993 at 9 (S.D. Ala. 1993).

Many states have established fraud divisions within their insurance departments, and some have enacted anti-fraud statutes, but none has even tried to occupy the field of legislation against insurance-related fraud. Indeed, not even the powerful assistance of the McCarran-Ferguson Act 15 U.S.C. § 1011 *et seq.* eliminates the need for state regulators to employ federal remedies for insurance fraud. The nationwide service of process available in civil RICO cases, 18 U.S.C. 1965, and the broad reach of federal criminal jurisdiction permit pursuit of complex, multi-jurisdictional frauds which would otherwise be unreachable in state court.

The availability of federal criminal and civil remedies for insurance fraud is indeed a matter of great national importance. The NAIC agrees, however, with the respondent herein that the decision of the Ninth Circuit, which is not contradicted by any authoritative precedent, is correct and does not require review. Therefore, the NAIC urges that the Court deny the petition for certiorari.

ARGUMENT

A.

THE NINTH CIRCUIT CORRECTLY OBSERVED THAT UNFAIR TRADE PRACTICES ACTS, SUCH AS CALIFORNIA'S UIPA, ARE MEANT TO SUPPLEMENT, NOT SUPERSEDE, PRIVATE RIGHTS OF ACTION.

In deciding that the application of RICO to an insurance dispute would not "invalidate, impair, or

supersede" any state law regulating the business of insurance within the meaning of McCarran-Ferguson, the Ninth Circuit correctly interpreted the intentions of the drafters of the Unfair Trade Practices Model Act. The interplay between various provisions of the Model Act and private causes of action has been the subject of extensive debate as the Model Act and its amendments have developed.

Since at least 1959, the Model Act and California's UIPA have included savings clauses for claims arising under other state law:

> No order to cease and desist issued under this article ... or subsequent administrative or judicial proceeding to enforce the same shall in any way relieve or absolve such person from any ...civil liability ... under the laws of this State arising out of the methods, acts, or practices found unfair or deceptive.

Cal. Ins. Code §790.09 (West 1995).

In the early 1970's, the NAIC considered amendments to the Model Act to expand the regulators' remedial options and to address unfair insurance claims settlement practices. One proposal would have allowed departments of insurance to bring class actions on behalf of injured consumers for relief from unfair practices. Another would have expanded the remedies available to the departments of insurance, once an unfair practice had been demonstrated, to include orders directing the guilty party to make restitution to those injured by its practices. An Industry Advisory Group successfully argued against the inclusion of "restitutionary" remedies in the new law contending that such remedies

were unnecessary because "persons injured have an adequate remedy at law," and that it was inappropriate to have the Commissioner of Insurance assume "a role that is usually the province of a jury -- that is, ascertain who may have been harmed and to what extent." Proceedings of the Laws, Legislation & Regulation Committee, 1972-1 NAIC Proc. 490 at 509 (1972).

The petitioners' argument to this Court, that the UIPA is such a comprehensive regulatory scheme that it would supersede existing private remedies, is flatly contradicted by both the text and the legislative history of the law. While it is true that no mention is made of uniquely federal remedies like RICO, nothing in the debates surrounding the Model Act suggests that the drafters meant to foreclose the enforcement of any private remedies for fraud, whether state or federal.

B.

THE DECISION OF THE NINTH CIRCUIT CONFLICTS WITH NO DECISION OF THIS COURT AND NO DECISION OF ANY OTHER FEDERAL COURT OF APPEALS.

The Ninth Circuit Court of Appeal undertook an analysis of whether the conduct complained of by the respondents involved the "business of insurance" within the meaning of McCarran-Ferguson, concluding that some did and some did not. That analysis, however, was mooted by its later conclusion that nothing in RICO "invalidated, impaired, or superseded" the UIPA. Petitioners' attempt to manufacture a conflict between this opinion and others focuses on the nature of the "business of insurance," but

ignores the court's overriding conclusion that no conflict exists between state law and RICO.

Interpretation of the term "business of insurance" is not uncomplicated. There is room for disagreement over its application to the facts of this case, and it is possible to identify real and imaginary conflicts among the cases discussing it. But under these circumstances, the issue is a red herring. Unless RICO "invalidates, impairs or supersedes" the California's UIPA, its application to the business of insurance, whatever that may be, is permitted by McCarran-Ferguson.

This Court has consistently ruled that the general provisions of McCarran-Ferguson apply only to laws which "directly conflict" with applicable state insurance law. *Securities & Exch. Comm'n v. National Securities, Inc.*, 393 U.S. 453 (1969); *United States Department of the Treasury v. Fabe.*, 113 S. Ct. 2202 (1993). The Seventh Circuit followed that rule in *NAACP v. American Family Mutual Ins. Co.*, 978 F.2d 287 (7th Cir. 1992), *cert. denied,* 113 S. Ct. 2335 (1993), and the Ninth Circuit in this case adopted the reasoning of the Seventh. There is no conflict between these cases.

Petitioners point to two state court decisions supposedly contradictory to the instant holding. However, one of them is an intermediate court decision whose principal rationale has been overruled by a later case in the state's Supreme Court.[4] The other, a decision of the intermediate court of

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[4] *American International Group v. Superior Court,* 234 Cal. App. 3d 749, 765-7, 285 Cal. Rptr. 765, 775-777 (2d

(continued...)

Pennsylvania, expressly identified its cursory conclusions concerning the conflict between RICO and state insurance law as *dictum*. *Leckey v. Aetna Casualty and Surety Co.*, 404 Pa. Super. 323, 590 A.2d 1255 (1991).

Petitioners point to a number of decisions of federal district courts which denied RICO relief to respondents defrauded by insurance related conduct. As support for their certiorari claims, these cases suffer from a number of defects:

1. Because they are trial court decisions, they present no ripe controversy to this court. (Supreme Court Rule 10)

2. Some of them apply laws which either contain the "restitution" provisions rejected by the drafters of the Model Act, *Everson v. Blue Cross & Blue Shield*, No. 93CV7534, 1994 WL 675200 (N.D. Ohio, Jun. 15, 1994); *Ambrose v. Blue Cross & Blue Shield of Va., Inc.*, 891 F. Supp. 1153 (E.D. Va. 1995), or lack the express savings clause contained in both the California law in issue here, and in the Model Act. *Wexco, Inc. v. IMC, Inc.*, 820 F. Supp. 194 (M.D. Pa. 1993); *Senich v. Transamerica Premier Insurance Co.*, 766 F. Supp. 339 (W.D. Pa. 1990); *Forsyth v. Humana, Inc.*,

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[4] (...continued)
Dist. 1991), *cert. denied,* 504 U.S. 911 (1992) assumed that California's UIPA superseded private remedies for the conduct proscribed by the law. If so, then federal remedies were likewise preempted. However, the California Supreme Court held the contrary, in *Manufacturers Life Ins. Co. v. Superior Court,* 10 Cal. 4th 257, 895 P.2d 56 (1995).

827 F. Supp. 1498 (D. Nev. 1993)), thus raising substantially different issues.

3. Others apply, to the general McCarran-Ferguson rule, the analysis applicable to the McCarran-Ferguson proviso for the Sherman, Clayton, and FTC Acts, *Gordon v. Ford Motor Credit Co.*, 868 F. Supp. 1191 (N.D. Cal. 1992); *Richhart v. Metropolitan Life Ins. Co.*, 1990 U.S. Dist. LEXIS 3597 (E.D. Pa. 1990), an error that is unlikely to be repeated in light of this Court's ruling in *United States Department of the Treasury v. Fabe.*, 113 S. Ct. 2202 (1993).

4. Several assume, contrary to fact, that the "comprehensive regulatory scheme" envisioned by the drafters of the insurance practices laws did not contemplate the survival of private civil remedies. *Wexco, Inc. v. IMC, Inc.*, 820 F. Supp. 194 (M.D. Pa. 1993); *Senich v. Transamerica Premier Insurance Co.*, 766 F. Supp. 339 (W.D. Pa. 1990); *Everson v. Blue Cross & Blue Shield*, No. 93CV7534, 1994 WL 675200 (N.D. Ohio 1994); *Ambrose v. Blue Cross & Blue Shield of Va.*, Inc., 891 F. Supp. 1153, (E.D. Va. 1995).

The "issue of nationwide importance" discovered by the petitioners, then, is a tempest in a teapot.

C.

PETITIONERS CANNOT COMPLAIN OF CONFUSION AND UNCERTAINTY AS TO THE REMEDY FOR THEIR CONCEDEDLY ILLEGAL AND FRAUDULENT CONDUCT.

It is common ground that, if the respondent has a case at all, it is based on fraud and outright theft by persons for whose actions the petitioners are liable. The serious betrayal of a customer's trust which the respondent alleges here deserves little protection from this, or any, court. The "confusion" and "uncertainty" to which the petitioners refer relates, not to the propriety of the conduct of their agents, but to whether this plaintiff can complain about it. As the California Supreme Court pointed out in a similar case:

> In essence, their claim is that they believed they could violate the law and be subject only to sanctions imposed by the Insurance Commissioner. Principles of *stare decisis* do not protect a person from the consequences of actions based on such a belief.

Manufacturers Life Insurance Company v. Superior Court, 10 Cal. 4th 257, 895 P.2d 56 (1995).

CONCLUSION

For all of these reasons, the National Association of Insurance Commissioners joins the respondent herein in opposing the petition for a writ of certiorari in this case.

Respectfully submitted,

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Dated: September 29, 1995

APPENDIX

NAIC Unfair Trade Practices Model Act

Proceedings of the National Association of Insurance Commissioners, 1972, Volume I

Regular Meeting, Miami Beach, Florida

November 28, 1971 - December 3, 1971

1972-1 NAIC Proc. 490

AN ACT RELATING TO UNFAIR METHODS OF COMPETITION AND UNFAIR AND DECEPTIVE ACTS AND PRACTICES IN THE BUSINESS OF INSURANCE

As adopted by the NAIC Laws, Legislation and Regulation (B) Committee.

SECTION 1 -- DECLARATION OF PURPOSE.

The purpose of this Act is to regulate trade practices in the business of insurance in accordance with the intent of Congress as expressed in the Act of Congress of March 9, 1945 (Public Law 15, 79th Congress), by defining, or providing for the determination of, all such practices in this state which constitute unfair methods of competition or unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined.

SECTION 2 -- DEFINITIONS.

When used in this Act:

(a) "Person" shall mean any individual, corporation,

association, partnership, reciprocal exchange, inter-insurer, Lloyds insurer, fraternal benefit society, and any other legal entity engaged in the business of insurance, including agents, brokers and adjusters. Person shall also mean medical service plans and hospital service plans as defined in Section. For purposes of this Act, medical and hospital service plans shall be deemed to be engaged in the business of insurance.

Drafting Note: This definition could also include dental, optometric, and other service plans. The enabling statutes of all service plans should also be amended to make them subject to this Act.

(b) ("Commissioner") shall mean the (Commissioner) of Insurance of this state.

(c) "Insurance policy" or "insurance contract" shall mean any contract of insurance, indemnity, medical or hospital service, suretyship, or annuity issued, proposed for issuance, or intended for issuance by any person.

Drafting Note. Each state may wish to consider the advisability of defining "insurance" for purposes of this Act if its present insurance code is not satisfactory in this regard. In some cases a cross reference will be sufficient. "Service contract" is intended to cover the product issued by medical and hospital service plans and should be changed to conform to the laws of each state.

NAIC Unfair Trade Practices Model Act

SECTION 3 -- UNFAIR METHODS OF COMPETITION AND UNFAIR OR DECEPTIVE ACTS OR PRACTICES PROHIBITED.

No person shall engage in this state in any trade practice which is defined in this Act as, or determined pursuant to Section 7 of this Act to be, an unfair method of competition or an unfair or deceptive act or practice in the business of insurance.

SECTION 4 -- UNFAIR METHODS OF COMPETITION AND UNFAIR OR DECEPTIVE ACTS OR PRACTICES DEFINED.

The following are hereby defined as unfair methods of competition and unfair or deceptive acts or practices in the business of insurance:

(1) **MISREPRESENTATIONS AND FALSE ADVERTISING OF INSURANCE POLICIES**. Making, issuing, circulating, or causing to be made, issued or circulated, any estimate, illustrations, circular or, statement, sales presentation, omission, or comparison which:

(a) misrepresents the benefits advantages conditions, or terms of any insurance policy; or

(b) misrepresents the dividends or share of the surplus to be received on any insurance policy; or

(c) makes any false or misleading statements as to the dividends or share of surplus previously paid on any insurance policy; or

(d) is misleading or is a misrepresentation as to the financial condition of any person, or as to the legal reserve system upon which any life insurer operates;

(e) uses any name or title of any insurance policy or class of insurance policies misrepresenting the true nature thereof

(f) is a misrepresentation for the purpose of inducing or tending to induce to the lapse, forfeiture, exchange, conversion, or surrender of any insurance policy; or

(g) is a misrepresentation for the purpose of effecting a pledge or assignment of or effecting a loan against any insurance policy; or

(h) misrepresents any insurance policy as being shares of stock.

(2) **FALSE INFORMATION AND ADVERTISING GENERALLY.** Making, publishing, disseminating, circulating or placing before the public, or causing, directly or indirectly, to be made, published, disseminated, circulated, or placed before the public, in a newspaper, magazine or other publication, or in the form of a notice, circular, pamphlet, letter or poster or over any radio or television station, or in any other way, an advertisement, announcement or statement containing any assertion, representation or statement with respect to the business of insurance or with respect to any person in the conduct of

his insurance business, which is untrue, deceptive or misleading.

(3) **DEFAMATION.** Making, publishing, disseminating, or circulating, directly or indirectly, or aiding, abetting or encouraging the making, publishing, disseminating or circulating of any oral or written statement or any pamphlet, circular, article or literature which is false, or maliciously critical of or derogatory to the financial condition of any person, and which is calculated to injure such person

(4) **BOYCOTT, COERCION AND INTIMIDATION.** Entering into any agreement to commit, or by any concerted action committing any act of boycott, coercion or intimidation resulting in or tending to result in reasonable restraint of, or monopoly in, the business of insurance.

(5) **FALSE STATEMENTS AND ENTRIES.**

(a) Knowingly filing with any supervisory or other public official, or knowingly making, publishing, disseminating, circulating or delivering to any person, or placing before the public, or knowingly causing directly or indirectly, to be made, published, disseminated, circulated, delivered to any person, or placed before the public, any false material statement of fact as to the financial condition of a person

(b) Knowingly making any false entry of a material fact in any book, report or statement of any person or knowingly omitting to make a true entry of any material fact pertaining to the business of such person in any book, report or statement of such person.

(6) **STOCK OPERATIONS AND ADVISORY BOARD CONTRACTS.** Issuing or delivering or permitting agents, officers or employees to issue or deliver, agency company stock or other capital stock, or benefit certificates or shares in any common-law corporation, or securities or any special or advisory board contracts or other contracts of any kind promising returns and profits as an inducement to insurance.

(7) **UNFAIR DISCRIMINATION.**

(a) Making or permitting any unfair discrimination between individuals of the same class and equal expectation of life in the rates charged for any contract of life insurance or of life annuity or in the dividends or other benefits payable thereon, or in any other of the terms and conditions of such contract.

(b) Making or permitting any unfair discrimination between individuals of the same class and of essentially the same hazard in the amount of premium, policy fees, or rates charged for any policy or contract of accident or health insurance or in the benefits payable thereunder, or in any of the terms or conditions of such contract, or in any other manner whatever.

Drafting Note: In the event that unfair discrimination in connection with accident and health coverage is treated in other statutes this paragraph should be omitted.

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(8) **REBATES.**

(a) Except as otherwise expressly provided by law, knowingly permitting or offering to make or making any contract of life insurance, life annuity or accident and health insurance, or agreement as to such contract other than as plainly expressed in the insurance contract issued thereon, or paying or allowing, or giving or offering to pay, allow, or give, directly or indirectly, as inducement to such insurance or annuity, any rebate of premiums payable on the contract, or any special favor or advantage in the dividends or other benefits thereon, or any valuable consideration or inducement whatever not specified in the contract; or giving, or selling, or purchasing or offering to give, sell, or purchase as inducement to such insurance contract or annuity or in connection therewith, any stocks, bonds, or other securities of any insurance company or other corporation, association, or partnership, or any dividends or profits accrued thereon, or anything of value whatsoever not specified in the contract.

(b) Nothing in clause (7) or paragraph (a) of clause (8) of this subsection shall be construed as including within the definition of discrimination or rebates any of the following practices:

(i) in the case of any contract of life insurance or life annuity, paying bonuses to policyholders or otherwise abating their premiums in whole or in part out of surplus accumulated from nonparticipating insurance, provided that any such bonuses or abatement of premiums shall be fair and equitable to policyholders and for the best interests of the company and its policyholders;

(ii) in the case of life insurance policies issued on the industrial debit plan, making allowance to policyholders who have continuously for a specified period made premium payments directly to an office of the insurer in an amount which fairly represents the saving in collection expenses;

(iii) readjustment of the rate of premium for a group insurance policy based on the loss or expense thereunder, at the end of the first or any subsequent policy year of insurance thereunder, which may be made retroactive only for such policy year.

Drafting Note: Each state may wish to examine its rating laws to assure that they contain sufficient provision against rebating. If they do not, this section might be expanded to cover all lines of insurance.

(9) **UNFAIR CLAIM SETTLEMENT PRACTICES.**

Committing or performing with such frequency as to indicate a general business practice any of the following:

(a) misrepresenting pertinent facts or insurance policy provisions relating to coverages at issue;

(b) failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies;

(c) failing to adopt and implement reasonable standards for the prompt investigation of claims arising under insurance policies;

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(d) refusing to pay claims without conducting a reasonable investigation based upon all available information;

(e) failing to affirm or deny coverage of claims within a reasonable time after proof of loss statements have been completed.

(f) not attempting in good faith to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear;

(g) compelling insureds to institute litigation to recover amounts due under an insurance policy by offering substantially less than the amounts ultimately recovered in actions brought by such insureds;

(h) attempting to settle a claim for less than the amount to which a reasonable man would have believed he was entitled by reference to written or printed advertising material accompanying or made part of an application;

(i) attempting to settle claims on the basis of an application which was altered without notice to, or knowledge or consent of the insured;

(j) making claims payments to insureds or beneficiaries not accompanied by statement setting forth the coverage under which the payments are being made;

(k) making known to insureds or claimants a policy of appealing from arbitration awards in favor of insureds or

claimants for the pourpose of compelling them to accept settlements or compromises less than the amount awarded in arbitration;

(l) delaying the investigation or payment of claims by requiring an insured, claimant, or the physician of either to submit a preliminary claim report and then requiring the subsequent submission of formal proof of loss forms, both of which submissions contain substantially the same information;

(m) failing to promptly settle claims, where liability has become reasonably clear, under one portion of the insurance policy coverage in order to influence settlements under other portions of the insurance policy coverage;

(n) failing to promptly provide a reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement.

(10) **FAILURE TO MAINTAIN COMPLAINT HANDLING PROCEDURES.** Failure of any person to maintain a complete record of all the complaints which it has received since the date of its last examination under S... This record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of these complaints, and the time it took to process each complaint. For purposes of this Subsection, "complaint" shall mean any written communication primarily expressing a grievance.

Drafting Note: Each state may wish to consider

exempting agents and brokers from this Subsection.

(11) **MISREPRESENTATION IN INSURANCE APPLICATIONS.** Making false or fraudulent statements or representations on or relative to an application for an insurance policy, for the purpose of obtaining a fee, commission, money, or other benefit from any insurers, agent, broker, or individual.

(12) Any violation of any one of Section

Drafting Note: Insert section numbers of any other sections of the Insurance Law which it is deemed desirable or necessary to include as an unfair trade practice.

SECTION 5. FAVORED AGENT OR INSURER; COERCION OF DEBTORS.

(a) No person may

(i) require, as a condition precedent to the lending of money or extension of credit, or any renewal thereof, that the person to whom such money or credit is extended or whose obligation the creditor is to acquire or finance, negotiate any policy or contract of insurance through a particular insurer or group of insurers or agent or broker or group of agents or brokers;

(ii) unreasonably disapprove the insurance policy provided by a borrower for the protection of the property securing the credit or lien; or

(iii) require directly or indirectly that any borrower,

morgagor, purchaser, insurer, broker, or agent pay a separate charge, in connection with the handling of any insurance policy required as security for loan on real estate, or pay a separate charge to substitute the insurance policy of one insurer for that of another.

(iv) use or disclose information resulting from a requirement that a borrower, mortgagor or purchaser furnish insurance of any kind on real property being conveyed or used as collateral security to a loan, when such information is to the advantage of the mortgage, vendor, or lender, or is to the detriment of the borrower, mortgagor, purchaser, insurer, or the agent or broker complying with such a requirement.

(b) (i) Paragraph a(iii) does not include the interest which may be charged on premium loans or premium advancements in accordance with the security instrument;

(ii) For purposes of par. (a)(ii), such disapproval shall be deemed unreasonable if it is not based solely on reasonable standards uniformly applied, relating to the extent of coverage required and the financial soundness and the services of an insurer. Such standards shall not discriminate against any particular type of insurer, nor shall such standards call for the disapproval of an insurance policy because such policy contains coverage in addition to that required.

(iii) The (Commissioner) may investigate the affairs of any person to whom this subsection applies to determine whether such person has violated this subsection. If a violation of this subsection is found, the person in violation

shall be subject to the same procedures and penalties as are applicable to other provisions of this Act.

(iv) For purposes of this section, "person" includes any individual, corporation, association, partnership, or other legal entity.

SECTION 6 -- POWER OF COMMISSIONER.

The (Commissioner) shall have power to examine and investigate into the affairs of every person engaged in the business of insurance in this state in order to determine whether such person has been or is engaged in any unfair method of competition or in any unfair or deceptive act or practice prohibited by Section 3 of this Act.

SECTION 7 -- DEFINED AND UNDEFINED PRACTICES: HEARINGS, WITNESSES, APPEARANCES, PRODUCTION OF BOOKS AND SERVICE OF PROCESS.

(a) Whenever the (Commissioner) shall have reason to believe that any such person has been engaged or is engaging in this state in any unfair method of competition or any unfair or deceptive act or practice whether or not defined in Section 4 or 5, and that a proceeding by him in respect thereto would be to the interest of the public, he shall issue and serve upon person a statement of the charges in that respect and a notice of a hearing thereon to be held at a time and place fixed in the notice, which shall not be less than days after the date of the service thereof.

(b) At the time and place fixed for such hearing, such person shall have an opportunity to be heard and to show cause why an order should not be made by the (Commissioner) requiring such person to cease and desist from the acts, methods or practices so complained of. Upon good cause shown, the (Commissioner) shall permit any person to intervene, appear and be heard at such hearing by counsel or in person.

(c) Nothing contained in this Act shall require the observance at any such hearing of formal rules of pleading or evidence.

(d) The (Commissioner), upon such hearing, may administer oaths, examine and cross-examine witnesses, receive oral and documentary evidence, and shall have the power to subpoena witnesses, compel their attendance, and require that production of books, papers, records, correspondence, or other documents which he deems relevant to the inquiry. The (Commissioner), upon such hearing, may, and upon the request of any party shall, cause to be made a stenographic record of all the evidence and all the proceedings had at such hearing. If no stenographic record is made and if a judicial review is sought, the (Commissioner) shall prepare a statement of the evidence and proceeding for use on review. In case of a refusal of any person to comply with any subpoena issued hereunder or to testify with respect to any matter concerning which he may be lawfully interrogated, the court of county or the county where such party resides, on application of the (Commissioner), may issue an order

requiring such person to comply with such subpoena and to testify; and any failure to obey any such order of the court may be punished by the court as a contempt thereof.

(e) Statements of charges, notices, orders, and otherprocesses of the (Commissioner) under this Act may be served by anyone duly authorized by the (Commissioner), either in the manner provided by law for service of process in civil actions, or by registering and mailing a copy thereof to the person affected by such statement, notice, order, or other process at his or its residence or principal office or place of business. The verified return by the person so serving such statement, notice, order, or other process, setting forth the manner of such service, shall be proof of the same, and the return postcard receipt for such statement, notice, order or other process, registered and mailed as aforesaid, shall be proof of the service of the same.

SECTION 8 -- CEASE AND DESIST AND PENALTY ORDERS AND MODIFICATIONS THEREOF.

(a) If, after such hearing, the (Commissioner) shall determine that the person charged has engaged in an unfair method of competition, or on unfair or deceptive act or practice he shall reduce his findings to writing and shall issue and cause to be served upon the person charged with the violation a copy of such findings and an order requiring such person to cease and desist from engaging in such method of competition, act or practice and if the act or practice is a violation of Sections 4 or 5, the (Commissioner) may at his discretion order any one or more of the following:

(A) payment of a monetary penalty of not more than $1000 for each and every act or violation but not to exceed an aggregate penalty of $10,000 *unless the person knew or reasonably should have known he was in violation of this Act, in which case the penalty shall be not more than $5000 for each and every act or violation but not to exceed an aggregate penalty of $50,000 in any six month period.*[1]

(B) suspension or revocation of the person's license if he knew or reasonably should have known he was in violation of this Act.[, or

(C) such other relief as is reasonable and appropriate.][2]

(b) Until the expiration of the time allowed under section 9 of this Act for filing a petition for review (by appeal or writ of certiorari) if no such petition has been duly filed within such time or, if a petition for review has been filed within such time, then until the transcript of the record in the proceeding has been filed in the court, as hereinafter provided, the (Commissioner) may at any time, upon such notice and in such manner as he shall deem proper, modify or set aside in whole or in part any order issued by him under this section.

(c) After the expiration of the time allowed for filing such a petition for review if no such petition has been duly filed

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[1] Material in italics added by the Laws, Legislation and Regulation (B) Committee.

[2] Material in brackets was deleted by the Law, Legislation and Regulation (B) Committee.

within such time, the (Commissioner) may at any time, after notice and opportunity for hearing, reopen and alter, modify or set aside, in whole or in part, any order issued by him under this section, whenever in his opinion conditions of fact or of law have so changed as to require such action or if the public interest shall so require.

SECTION 9 -- JUDICIAL REVIEW OF ORDERS.

Any person subject to an order of the (Commissioner) under section 8 or Section 11 may obtain a review of such order by filing in the court of county, within days from the date of the service of such order, a written petition praying that the order of the (Commissioner) be set aside. A copy of such petition shall be forthwith served upon the (Commissioner), and thereupon the (Commissioner) forthwith shall certify and file in such court a transcript of the entire record in the proceeding, including all the evidence taken and the report and order of the (Commissioner). Upon such filing of the petition and transcript such court shall have jurisdiction of the proceeding and of the question determined therein, shall determine whether the filing of such petition shall operate as a stay of such order of the (Commissioner), and shall have power to make and enter upon the pleadings, evidence, and proceedings set forth in such transcript a decree modifying, affirming or reversing the order of the (Commissioner), in whole or in part. The findings of the (Commissioner) as to the facts, if supported by evidence, shall be conclusive.

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Drafting Note: Insert appropriate language to accommodate to local procedure the effect given the Commissioner's determination.

(b) To the extent that the order of the (Commissioner) is affirmed, the court shall thereupon issue its own order commanding obedience to the terms of such order of the (Commissioner). If either party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for the failure to adduce such evidence in the proceeding before the (Commissioner), the court may order such additional evidence to be taken before the (Commissioner) and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The (Commissioner), may modify his findings of fact, or make new findings by reason of the additional evidence so taken, and he shall file such modified or new findings which if supported by evidence shall be conclusive, and his recommendation if any, for the modification or setting aside of his original order, with the return of such additional evidence.

Drafting Note: Insert appropriate language to accommodate to local procedure the effect given the Commissioner's determination. In a state where the final judgment, order to decree would not be subject to review by an appellante court provision therefor should be here inserted.

(c) An order issued by the (Commissioner) under section 8 shall become final:

(1) Upon the expiration of the time allowed for filing a petition for review if no such petition has been duly filed within such time; except that the (Commissioner) may thereafter modify or set aside his order to the extent provided in section 8(b); or

(2) Upon the final decision of the court if the court directs that the order of the (Commissioner) be affirmed or the petition for review dismissed.

(d) No order of the (Commissioner) under this Act or order of a court to enforce the same shall in any way relieve or absolve any person affected by such order from any liability under any other laws of this state.

SECTION 10 -- JUDICIAL REVIEW BY INTERVENOR.

If after any hearing under Section 7 or Section 11, the report of the (Commissioner) does not charge a violation of this Act, then any intervenor in the proceedings may within days after the service of such report, cause a petition (notice of appeal) (petition for writ of certiorari) to be filed in the court of county for a review of such report. Upon such review, the court shall have authority to issue appropriate orders and decrees in connection therewith, including, if the court finds that it is the interest of the public, orders enjoining and restraining the continuance of any method of competition, act or practice which it finds, notwithstanding such report of the (Commissioner), constitutes a violation of this Act and containing penalties pursuant to Section 8.

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Drafting Note: The type of procedure should conform to state procedure. See also note to Section 9 concerning review by appellate courts.

SECTION 11 -- PENALTY FOR VIOLATION OF CEASE AND DESIST ORDERS.

Any person who violates a cease and desist order of the (Commissioner) under section 8, and while such order is in effect, may after notice and hearing and upon order of the (Commissioner) be subject at the discretion of the (Commissioner) to any one or more of the following:

(a) a monetary penalty of not more than $10,000 for each and every act or violation; or

(b) suspension or revocation of such person's license.[; or

(c) such other relief as is reasonable and appropriate.][3]

SECTION 12 -- REGULATIONS.

The (Commissioner) may, after notice and hearing, promulgate reasonable rules and regulations, as are necessary or proper to identify specific methods of competition or acts or practices which are prohibited by Sections 4 or 5, but the regulations shall not enlarge upon or extend the provisions of Sections 4 and 5. Such

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[3] Material in brackets was deleted by the Laws, Legislation and Regulation (B) Committee.

regulations shall be subject to review in accordance with Section .

Drafting Note: Insert section number providing for review of administrative orders.

SECTION 13 -- PROVISIONS OF ACT ADDITIONAL TO EXISTING LAW.

The powers vested in the (Commissioner) by this Act, shall be additional to any other powers to enforce any penalties, fines or forfeitures authorized by law with respect to the methods, acts and practices hereby declared to be unfair or deceptive.

SECTION 14 -- IMMUNITY FROM PROSECUTION.

If any person shall ask to be excused from attending and testifying or from producing any books, papers, records, correspondence or other documents at any hearing on the ground that the testimony or evidence required of him may tend to incriminate him or subject him to a penalty or forfeiture, and shall notwithstanding be directed to give such testimony or produce such evidence, he must none the less comply with such direction, but he shall not thereafter be prosecuted or subjected to any penalty or forfeiture for or on account of any transaction, matter or thing concerning which he may testify or produce evidence thereto, and no testimony so given or evidence produced shall be received against him upon any criminal action, investigation or proceeding, provided, however, that no such individual so testifying shall be exempt from prosecution or punishment for any perjury committed by him while so testifying and

the testimony or evidence so given or produced shall be admissible against him upon any criminal action, investigation or proceeding concerning such perjury, nor shall he be exempt from the refusal, revocation or suspension of any license, permission or authority conferred, or to be conferred, pursuant to the Insurance Law of this state. Any such individual may execute, acknowledge and file in the office of the (Commissioner) a statement expressly waiving such immunity or privilege in respect to any transaction, matter or thing specified in such statement and thereupon the testimony of such person or such evidence in relation to such transaction, matter or thing may be received or produced before any judge or justice, court, tribunal, grand jury or otherwise, and if so received or produced such individual shall not be entitled to any immunity or privilege on account of any testimony he may so give or evidence so produced.

SECTION 15 -- SEPARABILITY PROVISION.

If any provision of this Act, or the application of such provision to any person or circumstances, shall be held invalid, the remainder of the Act, and the application of such provision to person or circumstances other than those as to which it is held invalid, shall not be affected thereby.

No. 95-409 (6)

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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1995

PROMETHEUS FUNDING CORP., etc., et al.,
Petitioners,
VS.
MERCHANTS HOME DELIVERY SERVICES, INC.,
Respondent.

SUPPLEMENTAL BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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THERE IS NOW CONFLICT AMONG THE COURT OF APPEALS FOR THE SIXTH, SEVENTH AND NINTH CIRCUITS OVER THE SCOPE OF PREEMPTION UNDER THE McCARRAN-FERGUSON ACT

Since the filing of the petition for certiorari, the Court of Appeals for the Sixth Circuit has decided *Kenty v. Bank One, Columbus, N.A.*, No. 93-4211, 1995 WL 621782 (6th Cir. Oct. 25, 1995), which squarely addresses the scope of preemption under the McCarran-Ferguson Act (15 U.S.C. § 1011 et seq.). *Kenty* follows the preemption analysis set forth in a line of cases exemplified by *Ambrose v. Blue Cross & Blue Shield of VA, Inc.*, 891 F. Supp. 1153 (E.D. Va. 1995), *Forsyth v. Humana, Inc.*, 827 F. Supp. 1498 (D.Nev. 1993), and *LeDuc v. Kentucky Cent. Life Ins. Co.*, 814 F. Supp. 820 (N.D. Cal. 1992). Consistent with this line of authority, *Kenty* holds that McCarran-Ferguson precludes application of the federal Racketeer Influenced and Corrupt

Organizations Act (RICO) to an insurance company engaged in the business of insurance.

As petitioners have demonstrated, the Ninth Circuit Court of Appeals here rejected the analytical approach of this same line of cases in favor of the sharply different preemption analysis contained in *NAACP v. American Family Mutual Ins. Co.*, 978 F.2d 287 (7th Cir. 1992), *cert. denied*, 113 S.Ct. 2335 (1993). (See Petn. for Cert. at pp. 12-13, 14-20)

Simply put, *Kenty* creates a conflict among the circuits over the scope of McCarran-Ferguson preemption. This conflict, together with the other reasons set forth in the petition for certiorari, justify this Court's intervention and review of the Ninth Circuit's opinion.

DATED: November 1, 1995.

CROSBY, HEAFEY, ROACH & MAY
Professional Corporation

By _____
James C. Martin
Attorneys for Petitioners